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THE CHINA BUSINESS REVIEW

THE MAGAZINE OF
THE US-CHINA BUSINESS COUNCIL

MARKETING FOR 2008

$ 2004

$ 2008

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Short Takes

China Ends a Chemical Era?

China and Venezuela pledged last month to phase out production of chlorofluorocarbons (CFCs), a family of ozone-depleting chemicals used primarily as coolant in refrigerators and air conditioners. China, one of the leading sources of black market CFCs, will eliminate CFC production by July 2007. The pledge will end the production of CFCs worldwide.

According to the World Bank, China is still the largest global producer and consumer of ozone-depleting substances, although it is working with the implementing arms of the Montreal Protocol to reduce its emissions of global pollutants.

Olympics to Open at a Fortunate Time

PRC officials are leaving nothing to chance, setting the opening of the 2008 Beijing Olympic Games for 8:00 pm on August 8, 2008. Eight (*ba*) is considered a lucky number in China because it sounds similar to "prosper" (*fa*). Officials originally planned to open the Olympics in late August because Beijing is unbearably hot earlier in the month, but moved the opening forward to avoid conflict with the US Open, which is scheduled for the end of August.

LeBron Wins but Nike Loses

In a pointed reminder on cultural sensitivity, China's State Administration for Radio, Film, and Television pulled a Nike television commercial from the airwaves, citing rules that require commercials to "protect national honor and traditional Chinese culture." The lesson: Be sensitive to national pride when picking advertising and media content.

The Nike "Chamber of Fear" advertisement, created by agency Wieden + Kennedy, showed National Basketball Association star LeBron James triumphing over animated, allegorical figures based on traditional Chinese figures, including a martial arts villain, two floating Chinese women throwing money, and two dragon-like monsters. The PRC government said the ad offended many Chinese viewers, presumably because it featured a foreigner handily defeating Chinese challengers.

Note from the Publisher: *CBR* Becomes a Frequent Flier

Starting with this issue, the *CBR* will circulate to first and business-class passengers on United, Northwest, Delta, Cathay Pacific, and Singapore airlines. By increasing airline circulation by more than 25 percent, *CBR* will reach more corporate decisionmakers involved with China than ever before. To find out more about becoming an advertising sponsor of the *CBR*, contact Jesse Marth (202-429-0340; jmarth@uschina.org).

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BULLETIN

EVENT WRAP-UP

Washington

November

Reception for the National People's Congress (NPC) Delegation Featured the Company Law and Securities Law Redrafting Delegation with members from the NPC, State Council, and China Securities Regulatory Commission (CSRC). Wu Gaosheng, director general, Research Office of the Legislative Affairs Commission of the NPC Standing Committee, led the delegation.

Issues Luncheon on China's Currency and Other Economic Issues: The Treasury View Featured US Department of the Treasury Office of East Asian Nations Director Robert Dohner for a discussion on China's currency and other economic issues.

December

USCBC Board of Directors' Meeting

Welcome Reception for Incoming USCBC President John Frisbie

Issues Luncheon on US Visas for China Business: Update on Policy and Practice Featured Deputy Assistant Secretary for Visa Services Janice Jacobs.

New York

November

USCBC Financial Services Group Meeting Featured the Company Law and Securities Law Redrafting Delegation with members from the NPC, State Council, and CSRC. Attendees discussed possible improvements to the PRC Securities Law and the role of foreign companies.

Beijing

December

Discussion on Trade Unions in Foreign-Invested Enterprises (FIEs) Featured Ma Jianjun, a partner in the Jun He Law Firm Shanghai office, for a discussion on the establishment of trade unions in FIEs and the legal requirements for companies under existing PRC trade union law.

Shanghai

December

Discussion on Trade Unions in FIEs Featured Ma Jianjun, a partner in the Jun He Law Firm Shanghai office.

UPCOMING EVENTS

Issues Luncheons, Washington, DC

February 17, 2005
March 17, 2005

China Business 2005

Chicago, Illinois: January 31, 2005
Dallas, Texas: February 1, 2005

Forecast 2005, Washington, DC

Evening Reception: February 2, 2005
Conference: February 3, 2005
For more information, see p.39

USCBC 32nd Annual Membership Meeting

Washington, DC: June 9, 2005

USCBC President John Frisbie

USCBC Board of Directors Convenes Biannual Meeting

(Left to right) USCBC President John Frisbie and USCBC Chair and UPS Chairman and CEO Michael L. Eskew; US Trade Representative (USTR) Robert Zoellick and Deputy USTR Josette Shiner at the USCBC Board of Directors Meeting.

The USCBC Board of Directors held its annual winter meeting in Washington, DC, on December 1, 2004. US Trade Representative (USTR) Robert Zoellick, Deputy USTR Josette Shiner, Assistant USTR for China Charles Freeman, and Assistant USTR for Intergovernmental Affairs and Public Liaison Christopher Padilla briefed the board on bilateral trade issues. The USTR team and the board then discussed intellectual property, PRC government procurement policy, currency issues, and trading and distribution rights for US companies in China and agreed to work closely on these and other issues in the coming year.

Reception Honors Incoming USCBC President John Frisbie

(Left to right) PRC Executive Vice Foreign Minister Dai Bingguo, Hebei Delegation Member Xu Shangwei, and Rep. John Shimkus (R-Illinois); guests at the reception; and Dai, Xu, and Eskew.

A reception to welcome USCBC President John Frisbie at the Smithsonian Institution's Sackler Gallery of Art immediately followed the board meeting. PRC Executive Vice Foreign Minister Dai Bingguo, who was in Washington, DC, for discussions with senior White House and Department of State officials; Rep. John Shimkus (R-Illinois); USCBC Chair and UPS Chairman and CEO Michael Eskew; and other speakers addressed roughly 300 guests, including representatives of more than 100 USCBC member companies. Other guests of honor included Rep. Henry Bonilla (R-Texas), PRC Ambassador Yang Jiechi, PRC Ministry of Foreign Affairs Department of American Affairs Director General He Yafei, and former US Ambassador to the PRC James Lilley.

Photographs: Kaveh Sardari

GOING FOR AN OLYMPIC MARKETING GOLD

China, and foreign companies, are learning marketing lessons from their predecessors

Scott Kronick and Dalton Dorne

Scott Kronick is managing director of Ogilvy Public Relations Worldwide, China.

Dalton Dorne is an associate, Corporate Communications, at Ogilvy & Mather China, Beijing.

Ogilvy worked with the Coca-Cola Co. and Swatch Group Ltd. in the run-up to the 2004 Olympic Games in Athens.

"Welcome to Beijing," uttered a young Chinese girl at the closing ceremony of the 28th Olympiad in Athens, Greece. Her message came just before the flame was lowered in Athens and was symbolic of the spirit in which Beijing is approaching the 2008 games.

If the Athens 2004 Olympics was Greece's opportunity to show the world the wonders of Greek culture, the Beijing Olympics is set to be China's debutante ball. The global spotlight during the next four years will shine increasingly on China and its preparations for the 2008 Olympics. No one understands this better than the Beijing Organizing Committee for the Games of the XXIX Olympiad (BOCOG). Hundreds of Chinese observers from a cross-section of government departments—including traffic management, security, sponsorship, and venue management—were present in Athens. Each PRC official had a specific role, and many were required to file reports upon their return from Greece.

"The Beijing Olympics will not be about sport, it will be about creating a superbrand called 'China,' and the brand essence is progress," commented one marketing expert in China. One thing is certain: The Beijing 2008 Olympic Games will be like none other, whether for "Brand China" or for marketers who participate.

The Olympics as a catalyst for change

When discussing the prospects for Beijing in relation to the Olympics, most observers cite what the Olympics achieved for cities such as Tokyo, Japan, and Barcelona, Spain. In 1964, at the beginning of Japan's technology revolution, observers credited the Olympics for sparking Japan's rapid consumer boom—Japanese raced out to buy TVs to watch the games. Barcelona, a sleepy provincial city in the 1980s, needed a prestige boost. The Barcelona organizing committee's campaign to make the city a star in 1992 succeeded. Event observers still remember the arrow that was shot to light the torch, the song "Barcelona," and the ceremony that celebrated the city. The Sydney 2000 games were similar, allowing Sydney to share its famous Australian hospitality with the world.

And in Athens, the 2004 Olympic Games achieved a number of records: "Most athletes in history. Most women [athletes] in history. Most national teams in history. First global torch relay. Safe and secure games, blessed by a climate of celebration and joy," listed Gianna Angelopoulos-Daskalaki, president of the Athens 2004 Organizing Committee for the Olympic Games. But Athens was also well known for barely meeting its Olympic infrastructure project deadlines.

In hindsight, the Athens Organizing Committee learned a valuable lesson about managing expectations in the lead-up to the games: The committee's failure to report infrastructure progress injured the reputation of the Athens organizers and of the city and country, to a degree. Only on the day before the games did Athens confirm for the press and the public that preparations were complete.

Beijing's moment

Clearly, BOCOG was studying Athens—and learning from its mistakes. The Athens Main Press Center opened less than one month before the 2004 games began. Beijing, however, established an Olympic News Center nearly four years before the 2008 Olympics. At the center's opening on November 1, 2004, BOCOG Vice President Jiang Xiaoyu announced in a *China Daily* article, "The media play an important role in the success of the Olympics...Beijing will draw on the experiences of previous games to provide high-quality services to the media."

BOCOG officials know it's not *what* it says, but *how* it says it, that matters and that it is crucial that the International Olympic Committee (IOC) support each statement. In a number of announcements recently reported in the media, BOCOG officials have reached out for IOC and public support by sharing both positive and negative updates on Olympic preparations. At one point BOCOG—together with IOC Coordination Commission President Hein Verbruggen—publicly announced the temporary halting of the construction of several venues to reevaluate design and construction costs.

Beijing has also identified themes for its 2008 Olympics: people, technology, and "Green Olympics." These are all farsighted themes for the overall improvement of the country. China's determination to be progressive and innovative is only growing stronger as the games approach—it is a chance for China to show that it is more than a manufacturing country.

- **People** This theme is part of a strong governmental push to work on social problems, such as poverty. The goal is to establish a greater economic balance, as a majority of Chinese citizens still have yet to benefit from China's economic progress—at least to the same extent as urban coastal dwellers.
- **Technology** China is abuzz about Beijing 2008 being the "high-tech Olympics." Du Zhanyuan, a planning official with the Ministry of Science and Technology, revealed that the government is spending up to $157 million and companies will contribute $217 million to 449 Olympic technology projects.
- **Green Olympics** Though the environment has been a theme of every Olympics since 1994, Beijing has reinforced the theme's importance by declaring the 2008 Olympics the "Green Olympics" (see the *CBR*, November–December 2003, p.16). The push for a Green Beijing and a Green Olympics has already begun—according to the *China Daily*, PRC officials plan to shut down or move out of Beijing more than 130 polluting enterprises by 2005.

Companies can build marketing campaigns around these themes by publicizing their corporate social responsibility leadership. For example, if companies support environmental conservation or education programs in impoverished regions of China, they should feature these programs in their advertising and marketing campaigns. High-tech companies should advertise that they are on the cutting edge.

Corporate participation

Beijing's selection as Olympic host has piqued the interest of global and national sponsors, companies with aspirations to influence the Olympic rings both internationally and locally. The motivation for sponsoring the Beijing Olympics is completely different from that of the Athens Olympics, one Athens sponsor notes. For instance, in Athens, sponsors were interested in the global platform the Olympics provided, but were not especially drawn by local market opportunities. In Beijing, sponsorship will have a double effect. First, a company that signs up for global sponsorship will be able to link with the Olympics, aligning its brand with Olympic ideals such as "excellence" and "victory" in

WISH TO SPONSOR IN 2008?

Olympic participation is divided into three levels: Olympic partners (who pay about $40 million), sponsors (who pay about $20-30 million), and service providers (companies that offer their services in exchange for sponsorship). The Beijing Organizing Committee for the Games of the XXIX Olympiad (BOCOG) plans to complete its Olympic partner plans by early 2005, and is currently looking for mobile equipment, truck transport, healthcare, and Internet partners. In early-to-mid-2005, BOCOG will begin looking for sponsors, followed by service providers. As these levels have yet to open, companies still have a chance to become official sponsors of the 2008 Olympics. BOCOG plans to have all three levels completed by 2007.

BOCOG Contacts

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General Office	86-10-6400-9185	xingzheng@beijing-olympic.org.cn
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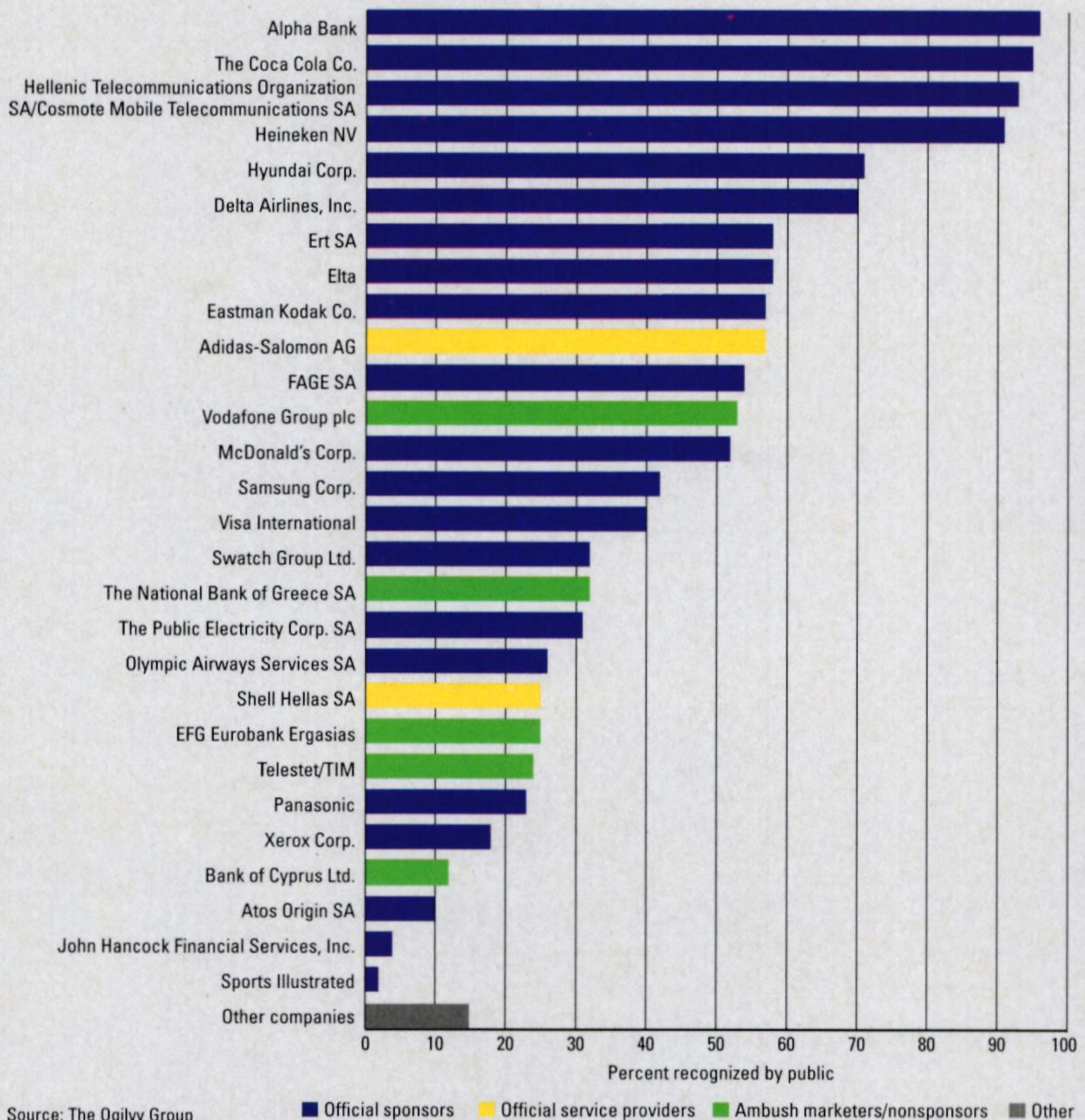
Marketing	86-10-6400-8322	shichang@beijing-olympic.org.cn
Information Center	86-10-6400-3598	xinxiguanli@beijing-olympic.org.cn

Sources: BOCOG; Ogilvy



its communications. Second, the company can strengthen its presence in the China market. As one Athens sponsor put it, "Few people are interested in securing greater depth in Greece, but everyone is interested in the opening up of China."

Momentum to secure sponsorship accelerated in 2003, when BOCOG invited companies from around the world to an Olympic marketing conference in Beijing that helped companies better understand how they could participate in the 2008 Olympics. BOCOG is currently deciding on numerous sponsors (see p.9).

Brands that become sponsors of the 2008 Olympics associate themselves not only with the Olympic ideals, but also with what the Olympics means to China; for China, the Beijing Olympics is about national pride, dignity, and progress. The Olympics gives Chinese brands an opportunity to enter the international arena and show the world what local brands are truly capable of. And for international brands, there is no better place than the 2008 Olympics to show commitment to China while building their presence in China.

Companies presently engaged in Olympic marketing—such as the Coca-Cola Co., Eastman Kodak Co., and McDonald's Corp.—already know the power of the games. In fact, Coca-Cola has been a sponsor since 1928. And these companies are all strong performers in China.

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Companies signed up, or planning to sign up for Olympic marketing, should consider three fundamental lessons:

1 Olympic sponsorship is a marathon, not a sprint

Historically, the more experienced sponsors begin their Olympic marketing efforts at least two years ahead of the games. For example, many 2004 Olympic sponsors began seriously marketing around the games in 2002. But some 2008 Olympic sponsors began their marketing efforts five years ahead of time. Companies that have signed up for sponsorship have formed teams to specialize in Olympic marketing efforts, and these teams have begun their work. Omega SA, for example, announced its official role as timekeeper for the Beijing Olympics by unveiling its countdown clock in Tiananmen Square. Coca-Cola has been marketing around the Beijing Olympics for more than a year, and it made Olympic marketing history on August 4, 2003 when it unveiled a specially designed can to commemorate Beijing's win of the Olympics. (The red and gold can, which has a silhouette of Beijing's Temple of Heaven in the background, is entirely in Chinese and shows both the Olympic rings and the Beijing Olympic symbol.)

The point, whether a company is an official Olympic sponsor or not, is to begin early. According to Coca-Cola, the company began plans for the Beijing commemorative can nearly five years before the city was even awarded the games.

2 Promote your sponsorship at multiple points of contact

Olympic sponsorship goes much further than advertising in advance of the games or devising ways to show customer hospitality during the games. Successful sponsorship takes on a campaign mentality that forms around a central idea and uses every point of contact the brand has with a consumer.

Coca-Cola understands this well. Not only does it create customized packaging that reinforces its sponsorship, but the company's advertising, website, merchandizing, and public relations all reinforce its Olympics sponsorship and its tie to Olympic ideals. For the games in Athens, Coca-Cola sponsored the 27-country torch relay, which marked the first truly global relay. The company leveraged its sponsorship throughout, culminating in a multifaceted Olympic pin-trading center designed in the shape of a Coke bottle (see photos). From this center, Coca-Cola provided entertainment, opportunities for journalists to broadcast to their audiences, and a host of interactive activities in and around the center.

Alpha Bank, the official bank of the 2004 Olympics, adopted a similar strategy. Positioning itself as the bank for people from all walks of life, the bank worked with federations of lesser-known sports to introduce these sports to the people of Greece and Cyprus. Through a series of direct marketing efforts, advertising, and road shows, Alpha Bank succeeded in making the most of its sponsorship. This culminated with an interactive event for visitors to the Olympics, during which consumers were able to experience the lesser-known sports first hand.

Don't Try This in China

The PRC Advertisement Law, which took effect in February 1995, prohibits the use of certain themes in advertising. Advertisements must not

- Contain China's national flag, emblem, or anthem
- Use the names of state organs or their functionaries
- Make claims such as "state-level," the "highest-grade," or the "best"
- Hinder social stability or harm public interest
- Violate PRC social customs
- Use pornography, superstition, terror, or violence
- Discriminate based on ethnicity, race, religion, or sex
- Harm the environment or natural resources
- Create circumstances prohibited by law

—*Scott Kronick* and *Dalton Dorne*

3 Be innovative

Athletes are not the only competitors in the Olympics—companies face intense competition as well, and consequently must come up with innovative marketing campaigns. Adidas-Salomon AG communicated its slogan, "Impossible is nothing," throughout Asia, celebrating the Olympic spirit with impossible sprints up skyscrapers in Osaka, Japan, and Hong Kong in August 2004. The amazing display served as a platform to connect Adidas's Olympic sponsorship to a global audience via local, regional, and international media reporting on the event.

In Greece, the Eastman Kodak Co. engaged consumers throughout the country in a photo project, in which Greek citizens took photos of themselves at Kodak centers. The compilation made up the largest photographic collage ever created, captured the Olympic spirit, and involved people from all over Greece. The press and the public gave Swatch Group Ltd., the official timekeeper of the 2004 Olympics, high praise in Athens for its artistic decoration of an entire street, known as the Swatch Iconic Centre, with Olympic memorabilia. The center hosted numerous cultural activities and events.

Restrictions on marketing activities during the games also force marketers to be more creative to get their message across. Coca-Cola found a way into the Olympic venues, a location where corporate branding was forbidden, with its big, red foam Coca-Cola hands. These applause-worthy pieces entered venues with sports fans who used them to cheer.

May the best marketing strategies win

The run-up to the Beijing Olympics will be competitive for marketers. Firms must therefore be creative to stand out. Brands, marketers, and sponsors must adopt, as Adidas has, an attitude that "Impossible is nothing."

The euphoria has begun, and the little girl at the closing ceremonies in Athens has spoken. Whether it is for the prospects of "China Inc.," for brands that are lining up to participate, or for those that may attempt an ambush marketing effort (when competitors of official sponsors find ways to associate their brand with the event), 2008 is on the minds of many in China.

In the same way the Olympics in Beijing will showcase China, world-class brands will showcase their world-class marketing strategies in China—and this may resonate with an increasingly sophisticated consumer base. 完

The Coca-Cola Co.'s 2004 Olympics pin-trading center.
Photographs: Courtesy of Ogilvy

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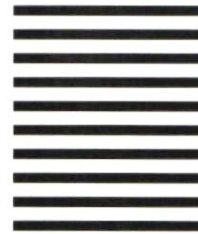
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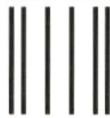

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ACQUISITIONS IN CHINA: Closing the Deal

Acquisition strategy, negotiation, and approval

Kim Woodard and
Anita Qingli Wang

Many international companies have developed in the China market to the point where they are now examining acquisition of a local company as a way to grow. The most fundamental strategic choice is, of course, whether to acquire at all. Building a grassroots, wholly owned business in China has become the most common and potentially most profitable investment alternative in a wide array of industries (see the *CBR*, September–October 2004, p.6). But in China's highly fragmented and competitive markets, a new business can take 5 to 10 years to achieve profitable scale. Acquisition of a well-positioned local company may be more difficult in the beginning, but may yield a sizeable increase in market share, an existing platform of domestic customers, lower costs, broader distribution, and elimination of a key competitor.

Acquisition is a promising option when

- Products or services are in a traditional sector with well established domestic competitors;
- The acquisition would cause a quantum jump in domestic market share for a strategic product or service type;
- Domestic competitors are beginning to export to core markets;
- Technology and intellectual property rights are not major concerns;
- There are state-mandated regulatory barriers to market access;

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A companion article on acquisition trends appeared in the November–December 2004 issue of the *CBR*.

Case 1: Hongkong and Shanghai Banking Corp. (HSBC)

Major acquisitions:

- Purchase of 8 percent of Bank of Shanghai through an increased capital subscription for $62.6 million in December 2001
- Acquisition of 50 percent of Fujian Asia Bank (now Ping An Bank) for about $20 million in 2003. HSBC now holds 27 percent because of a subsequent Ping An Insurance capital injection to Ping An Bank
- Acquisition (through Hang Seng Bank) with the Singapore Government Investment Corp. and the International Finance Corp. of 15.98 percent of Xingye Bank in Fujian for $208.7 million through an increased capital subscription in December 2003
- Purchase of 19.9 percent of Bank of Communications for $1.7 billion through an increased capital subscription in August 2004

Description: HSBC is taking stakes in China's banking and insurance industries by contributing new capital to domestic financial institutions. HSBC is using its acquisition program to pursue an aggressive strategy that takes advantage of the opening of retail banking and insurance to foreign investors. This strategy allows HSBC to work within mandated equity limits, while laying down an extensive service and branch structure in preparation for future expansion.

- There is an attractive field of available and willing mid-sized acquisition targets.

The second basic issue is whether to undertake an equity acquisition or an asset acquisition. In an equity acquisition, the foreign company takes part or full ownership of the target company's assets and liabilities. In an asset acquisition, the acquirer takes only the core business, leaving peripheral and nonperforming assets and liabilities to be restructured by the previous owner.

Many equity acquisitions are converted to asset acquisitions during the due diligence phase, when hidden operating weaknesses and liabilities are revealed. Clearly there are both financial and operating advantages in leaving unwanted assets, redundant employees, bad loans, and contingent liabilities behind. Experienced attorneys report, however, that asset acquisitions are more complex and take longer to complete than equity acquisitions. Most acquisitions of more than $50 million are in fact equity or stock acquisitions, while small and mid-sized acquisitions tend to be converted to asset acquisitions. An equity acquisition may be appropriate when

- The target company is listed;
- The foreign company can acquire the target company offshore or through acquisition of an offshore holding company;
- The foreign company wants a minority equity position in the acquired business;
- The government has mandated limits on foreign equity ownership, which would allow only partial acquisition;
- The local government and existing management refuse to consider an asset acquisition;
- Local and national approval authorities refuse to allow the company to be broken up;
- The acquirer is a financial investor, such as a foreign private equity fund.

Finally, companies must decide whether to finance the acquisition internally or seek an external investment partner. Large multinationals often have enough access to internal capital and bank loans to finance investment projects in China. But external investment partners may bring mergers and acquisitions (M&A) expertise to the table, including skills in selecting, negotiating, and restructuring the target company. Domestic Chinese investment partners may also be needed if there are mandated equity limits on foreign investment in the target sector.

Conversely, foreign financial investors, such as global and regional private equity funds, the investment arms of regional banks, and investment banks are increasingly leading acquisitions in China (see the *CBR*, July–August 2004, p.48). In cases requiring post-acquisition restructuring, private equity investors may want the help of corporations that bring global distribution, process and product technology, and world-class operating management to the table.

Case 2: Wanxiang Group

(Wanxiang is a leading privately owned conglomerate based in Zhejiang with a core business in brakes and other automotive parts.)

Acquired company: Universal Automotive Industries, Inc. (UAI)
Transaction value: $2.8 million
Transaction type: Acquisition of 21 percent of US listed company
Closing date: August 2001

Description: Wanxiang acquired a controlling interest in Nasdaq-listed UAI to create an indirect sourcing and distribution channel that would increase its auto parts exports to the United States. UAI is located in Chicago, Illinois, and produces brake parts. UAI was founded in 1981 and has faced increasing cost competition from China-based suppliers, such as Wanxiang. The strategic alliance with Wanxiang strengthens UAI's competitive position by reducing unit costs and strengthens Wanxiang by increasing access to UAI's customers.

The acquisition process—what to expect

Once the company has decided to proceed, an average-sized acquisition (roughly $20 to $50 million) will take about nine to twelve months from start to finish. Target selection and negotiation of a letter of intent will take three to four months, separate private and mandatory government due diligence will add two months, acquisition negotiations will take two to three months, and government approvals and formal closing will add a final two to three months.

Typical external acquisition costs (excluding internal management time and travel) will run from $500,000 to $2 million and can be significantly higher for larger or more complex acquisitions that involve an investment bank. Acquisition costs therefore can easily represent 10 to 20 percent of a

$5 million to $10 million acquisition. The time, cost, and risk analysis required for acquisition may decrease the relative value of a small acquisition.

Sufficient time and effort should be devoted to identification and selection of the acquisition target to ensure a strategic fit and reasonable probability of successful integration. Start with your own strategic objectives, products, market positions, and distribution requirements and screen nationally for the top three to five acquisition candidates. The State Asset Supervision and Administration Commission [SASAC], the Great Western Development Strategy and Revitalize the Northeast initiatives, and provincially administered property trading rights centers all publish lists of state-owned enterprises (SOEs) that are available for foreign investment or acquisition. But most companies look for targets that are market leaders instead of scanning such lists for fire-sale opportunities.

Once an appropriate acquisition target has been identified and selected, *willingness to be acquired* must be established at several levels. In the case of privately owned target companies, the owners and key managers are identical and local government involvement is minimal. In the case of SOEs, however, the protracted courting and negotiating process is reminiscent of the old joint venture negotiation dance. For most SOE assets, the provincial SASAC is now the equity owner and will make the final decision to divest the asset. Many local SOEs are now also part of a larger state-owned group company, in which case the group company will always be present at the negotiating table and may become the main negotiating partner. The local government industry bureau will also likely be involved, although it no longer formally "owns" the target company.

Willingness to be acquired often depends upon the intensity of resistance from the existing SOE management. Senior SOE executives were often appointed by the local government industry bureau, and they enjoy substantial status in the local community and other perquisites as a result of their positions. More aggressive SASACs in some provinces will sometimes push enterprise management into a deal that it would otherwise reject. For example, debt restructuring and approval for new working capital loans may be made contingent on sale of the SOE. Such inducements leave management with a choice between being acquired and slow starvation.

The national regulations on acquisition of listed SOEs also require a formal bidding process, and some localities, such as Beijing, have established "equity exchange centers" for this purpose (see the *CBR*, November–December 2004, p.40). While these requirements improve transparency, they do not preclude private overtures and negotiations between the acquiring party and the target company and its owners. In some cases, a letter of intent for the acquisition has even been signed before the public notification. This does not mean, however, that there is no competition for the asset. There is sometimes intense competition among domestic and foreign suitors, and the provincial SASAC usually has enough buyers to pick on the basis of pricing, technological prowess, management capabilities, and other criteria.

Government Review and Approval Authorities

Offshore	FIE	Private Enterprise	SOE	Listed SOE
SAFE	MOFCOM	MOFCOM	SASAC	SASAC
SAT	SAIC	SAIC	MOFCOM	MOFCOM
	SAFE	SAFE	NDRC*	CSRC
	SAT	SAT	SAIC	NDRC*
			SAFE	SAIC
			SAT	SAFE
				SAT

Formal approval required (shown in red)
Review for regulatory, tax, and foreign exchange compliance

LOW ← Level of Difficulty → HIGH

*NDRC review and approval is required for acquisition projects with national strategic impact, such as projects in "pillar industries," projects on the "restricted" list of the Catalogue Guiding Foreign Investment in Industry, projects with a significant impact on a single sector, and projects with gross assets of more than ¥400 million ($48 million).

Notes: CSRC=China Securities Regulatory Commission; FIE=foreign-invested enterprise; MOFCOM=Ministry of Commerce; NDRC=National Development and Reform Commission; SAFE=State Administration of Foreign Exchange; SAIC=State Administration for Industry and Commerce; SASAC=State Asset Supervision and Administration Commission; SAT=State Administration of Taxation; SOE=state-owned enterprise.

Source: Javelin Investments research

Key negotiating issues

Acquisition contract negotiations tend to focus on three major issues: valuation, debt restructuring, and size of the workforce. Independent asset valuation must result in a

Case 3: Thomson Corp.

Acquired company: Fudi Technology, one of the leading cathode ray tube (CRT) manufacturers in China
Transaction value: $80.8 million
Transaction type: Asset acquisition from listed SOE
Closing date: July 18, 2003

Description: Thomson acquired three color television CRT production lines and related facilities from Fudi Technology in Dongguan. Prior to the acquisition, Fudi had lost $48 million in its Dongguan CRT operation. Thomson already had five electronics production bases in China—four in Guangdong (Shenzhen, Foshan, Dongguan, and Guangzhou) and one in Beijing. Thomson added the Fudi CRT plant to its existing CRT factory in Foshan, increasing its capacity while eliminating a leading local competitor.

In order to sustain the value of Fudi as a listed company, the Dongguan government injected a new and unrelated asset—the Shenzhen-Dongguan Expressway—into Fudi.

Case 4: Amazon.com

Acquired company: Joyo.Com, an offshore private company
Transaction value: $75 million ($72 million in cash + $3 million in stock options)
Transaction type: Acquisition of 100 percent of privately owned company
Announcement date: August 19, 2004

Description: The acquisition of a privately owned Internet company gives Amazon access to the China business-to-consumer (B2C) market. Joyo.Com is the second-largest B2C retail company in China and sells books, audiovisual products, toys, cosmetics, and other consumer products. Joyo.Com has 80 million customers and annual revenues of $20 million. The Amazon-Joyo.Com acquisition follows two other major acquisitions in the Internet sector: Ebay acquired Eachnet in March 2002 ($30 million, or 33 percent equity); Yahoo acquired 3721.Com ($120 million, or 100 percent equity) in 2003.

Amazon first approached Dangdang.Com, the top player in the B2C retail space and Joyo.Com's largest competitor, offering $150 million for 70-90 percent of Dangdang's equity. Dangdang management, which believes the company can list or sell for a larger return within a few years, turned down the Amazon offer.

figure at or near net asset value (NAV), which must be set by a state-approved assets-valuation accountant. Heavy working capital debt, unrecoverable receivables, tax liabilities, and other current and contingent liabilities bring the NAV down significantly. This means that many equity acquisitions are made at a relatively low price compared to the value of the business as reflected by discounted cash flow or prevailing stock market multiples for comparable businesses.

Despite the low acquisition prices, these liabilities are probably the leading cause of negotiation failure and are also the main reason that deals that begin as equity acquisitions often end as asset acquisitions. The more aggressive provincial SASAC bureaus increasingly recognize that they cannot expect acquiring companies to shoulder decades of liability accumulation and will sometimes offer to restructure debt prior to the acquisition. The large state banks, however, must protect their books and will often resist SASAC's attempts to let the acquiring party off the hook.

Workforce redundancy is another deal-breaking issue. For example, the effort by LaFarge SA, a leading French cement maker, to acquire the two largest cement producers in Yunnan foundered on the status of several thousand redundant workers. Resolution of the workforce issue depends almost entirely on cooperation from the local government. In some cases, the local government will work with SASAC and the buyer to shrink employment at the target company prior to the acquisition. In other cases, the local government will accept a per capita payment from the buyer as part of the acquisition deal and will then make the layoffs and subsequent social benefit payments. Neither solution will change the local workforce's perception that the foreign investor "caused" the layoffs and/or the reduction or termination of pension and medical benefits.

Government approvals and closing the deal

All acquisitions of companies that are operating in China are subject to some level of official review or approval by local, provincial, and national government authorities. But the complexity, difficulty, and time required to complete the government review and approval process vary greatly by the type of acquisition target, the size of the acquisition transaction, and the impact on the industry and sector involved (see p.15).

An acquisition deal in China cannot formally "close" until all relevant government approvals and licenses have been issued. This not only creates a lag of a few months to a year or more in the closing and restructuring, but also causes timing problems with capital injection and enterprise restructuring. There is no effective escrow mechanism available under PRC commercial law that allows the buyer and seller to fully commit resources when the deal is finalized and signed, before required government approvals are complete. Milestone payments or restructuring and refinancing commitments on either side are therefore difficult to execute until government approvals are complete.

The regulatory environment

Acquisition of a domestic Chinese company, whether private, foreign-invested, state-owned, or listed, is subject to a growing body of legal and tax regulations (see p.17). While specific rules may be restrictive, the new regulations, as a whole, help legitimize and extend the options available to foreign corporations and investment funds seeking acquisition opportunities in China. Analysis of the specific provisions of regulations affecting M&A deals in China is best left to experienced legal and tax experts, but a few unique elements of China's M&A environment are worth noting.

The Chinese government and media have become increasingly sensitive to concentration and potential domination by foreign investors of

Case 5: Citibank NA

Acquired company: Shanghai Pudong Development Bank (SPDB)
Transaction value: $67 million
Transaction type: Acquisition of 4.62 percent of listed state-owned enterprise
Closing date: October 2003

Description: Citibank's acquisition of SPDB shares is part of its strategic thrust into the China retail banking and credit card sector. In an unusual move, Citibank was approved to purchase state-owned and legal person shares in a listed company from the Shanghai SASAC and from Shanghai Jiushi Corp. On February 4, 2004, the first Visa cards with the logos of both Citibank and SPDB were issued.

Selected PRC Regulations Governing Mergers and Acquisitions by Foreign Companies

Regulation	Issued by	Date Issued/Date Effective	Features
Measures for Administration of the Acquisition of Listed Companies	CSRC	September 28, 2002 December 1, 2002	• Modifies and elaborates 1999 Securities Law to regulate all acquisitions (i.e., by both domestic and foreign investors) of companies listed on China's stock exchanges. • Sets equity stake of 30% or more of a listed company as trigger for mandatory public offer for 100% of the company.
Notice on Transfer of Listed State-Owned Shares and Legal Person Shares to Foreign Investors	CSRC MOF SETC	November 1, 2002 January 1, 2003	• Governs the sale of state-owned shares and legal person shares in listed companies to foreign investors. • Fails to provide for the conversion of state-owned shares and legal person shares to listed shares, thereby blocking divestment of such shares on public stock markets.
Provisional Rules on the Management of Investment in Domestic Securities by Qualified Institutional Investors	PBOC CSRC	November 5, 2002 December 1, 2002	• Governs purchase of domestic A shares on local stock markets by qualified foreign institutional investors (QFII). • Sets equity limits (10% per QFII, 20% total foreign investment) and lock-up periods for such purchases.
Provisional Rules on the Use of Foreign Investment to Restructure State-Owned Enterprises	SETC MOF SAIC SAFE	November 8, 2002 January 1, 2003	• Governs assignment and sale of state-owned property rights, debt restructuring, and labor force restructuring in state-owned enterprises by foreign investors.
Provisional Rules for Mergers with and Acquisitions of Domestic Enterprises by Foreign Investors	MOFTEC* SAT SAIC SAFE	March 7, 2003 April 12, 2003	• Consolidates and clarifies pre-existing regulations and administrative rules on foreign merger and acquisition transactions. • Distinguishes equity acquisitions from asset acquisitions. • Establishes rules for third-party appraisal, registered capital ratios, approval authority, and other rules for acquisition by foreign investors of "domestic enterprises," including nonlisted SOEs and privately owned businesses.
Notice on Certain Tax Issues Concerning the Acquisition of Equity Interest in Domestic Enterprises by Foreign Investors	SAT	May 28, 2003 January 1, 2003	• Specifically extends foreign-invested enterprise (FIE) tax benefits to FIEs that are formed as the result of a merger or acquisition. • Includes initial two-year corporate income tax holiday, subsequent 50% tax reduction for three years, and loss carry-forward provisions.

*Now Ministry of Commerce

Notes: This list includes only the major regulations on acquisitions. Other laws and regulations, administrative and tax rules, and notices may affect specific acquisition deals. CSRC=China Securities Regulatory Commission; MOF=Ministry of Finance; MOFTEC=Ministry of Foreign Trade and Economic Cooperation; PBOC=People's Bank of China; SAIC=State Administration for Industry and Commerce; SAFE=State Administration of Foreign Exchange; SAT=State Administration of Taxation; SETC=State Economic and Trade Commission.

Sources: O'Melveny & Myers LLP; Paul, Weiss, Rifkind, Wharton & Garrison; Javelin Investments research

some domestic markets, such as mobile phones, photographic film, and soft drinks. Antitrust concerns will slow the government approval process, but will not necessarily result in government rejection of the deal (see the *CBR*, May–June 2004, p.60). For example, in October 2003 Eastman Kodak Co., which had already acquired three of four domestic photographic film producers and a dominant position in the photographic film market, was allowed to acquire 20 percent of Lucky Film, the remaining domestic film company.

The nontradability of state-owned and legal person shares also limits exits for foreign private equity funds or domestic Chinese investment groups doing buyouts in China, since investors usually gain control of listed SOEs via acquisition of these shares. Part of the failure of D'Long International Strategic Investment Co. was due to its inability to sell legal person shares in any of its six listed subsidiaries to raise cash and reduce debt. Foreign private equity has been slow to develop in China (and in Asia more generally) primarily because of this low liquidity in public stock markets and low price-to-earnings multiples in private trade sales (see the *CBR*, July–August 2004, p.48). The China Securities Regulatory Commission, fearing a flood of legal person share sales on domestic stock markets should this restriction be removed, shows no sign of moving on this key issue.

Paying taxes

Acquisitions that result in a foreign stake of 25 percent or more qualify for regular foreign-invested enterprise (FIE) tax benefits. Of continuing concern are the taxes that apply to M&A transactions, which include

- Stamp tax on the value of the transaction: 0.05 percent, applicable to both seller and buyer on equity and asset acquisitions;

Continued on page 35

Cooperative Joint Ventures

Savvy foreign investors may wish to consider the benefits of this flexible investment structure

Paul H. Folta

Despite the attractiveness of China's business and foreign investment environment, the country is not an easy place to do business. Foreign businesses that seek to enter the China market must consider a wide range of strategies and business structures—each with its own advantages and disadvantages.

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Since China's World Trade Organization (WTO) entry and the PRC government's relaxation of investment regulations, foreign investors have been choosing to establish more wholly foreign-owned enterprises (WFOEs), which in the first three quarters of 2004 made up nearly 67 percent of the value of new foreign direct investment projects in China (see Table). WFOEs cannot be used in every sector, however, because the PRC government requires Chinese company participation or control in some sectors. In such cases, foreign companies must consider a joint venture structure. Even when they are not required, joint ventures can benefit foreign investors when a Chinese partner has certain strengths—such as central or local government support, brand reputation, land, licenses, distribution, and access to suppliers—that reduce start up costs and improve the foreign investor's chances of success (see p.20).

In China, most joint ventures are equity joint ventures (EJVs), though some investors establish cooperative (or contractual) joint ventures (CJVs). CJVs and EJVs are similar in many respects. The PRC government approval process, approval authorities, format of agreements, tax breaks, legal standing, and the means, laws, and authorities for dispute resolution are identical. The general management structure and governance procedures are also virtually the same.

But CJVs and EJVs differ in two important ways. First, unlike an EJV, a CJV does not need to be a separate legal person under PRC law. (A CJV that is not a separate legal person may benefit from lower costs, but also may expose the parties to greater liability than if they were legal

In a CJV, Chinese partners can hold and "lend" assets and licenses that are forbidden to foreign investors under PRC law.

China's Foreign Direct Investment (Utilized FDI)

	2000	2001	2002	2003	Jan.–Sept. 2004
Total FDI ($ billion)	40.7	46.9	52.7	53.5	48.7
Wholly foreign-owned enterprises (%)	46.9	50.3	60.2	62.4	66.8
Equity joint ventures (%)	35.8	34.7	28.4	28.6	26.9
Cooperative joint ventures (CJV, %)	15.9	12.9	9.6	7.2	5.2
Other (%)	1.4	2.1	1.8	1.8	1.1
Approved CJV Projects (No.)	1,755	1,589	1,595	1,547	996

Note: Other=Share-based enterprises with foreign investment; and cooperative development vehicles
Sources: PRC Ministry of Commerce, the US-China Business Council

persons, because CJVs with legal person status confer limited liability on parties to the joint venture.) Second, the CJV parties' profit, control, and risks are divided according to negotiated contract terms. In contrast, an EJV's profit, control, and risk are divided in proportion to the equity shares invested by the parties.

CJV disadvantages

As is true for any investment structure, CJVs have their drawbacks. First, since all CJV contract details need to be negotiated, establishing a CJV can be time consuming and expensive. Indeed, CJV negotiations can derail potential ventures as parties discover that they cannot reach agreement on every detail. Second, CJVs are sometimes not the most appropriate business structure for the project. For example, a Western automotive technology company recently signed a memorandum of understanding for a CJV with a Chinese state-owned enterprise (SOE) for the manufacture and sale of its patented system in China. The venture did not proceed, however, because the SOE ultimately determined that it preferred an EJV so that profit sharing ratios would match shareholdings and future changes in registered capital. In the end, the foreign company decided to form a WFOE, but planned to maintain and develop options to work with its Chinese partners in the future.

Why choose a CJV?

CJVs nevertheless can offer investors several advantages. Compared to EJVs, cooperative joint ventures

- **Allow access to restricted sectors**

In a CJV, Chinese partners can hold and "lend" assets and licenses that are forbidden to foreign investors under PRC law, or that are undesired by the foreign partner, until the venture terminates or foreign ownership rules are relaxed. Undesirable assets may include those with a high transfer tax, or those that are too complicated or costly for the foreign investor to obtain, such as land. For example, a Chinese company can "lend" its license to a CJV in a value-added telecom network (see p.22). A Chinese company would not be permitted to transfer such a license to an EJV because the license, if forbidden to foreign owners, would be considered part of the whole company's assets.

A CJV could also allow negotiated levels of management and financial control, as well as methods of recourse associated with equipment leases and service contracts; in an EJV, foreign investors cannot always obtain such control since EJVs typically rely on equity levels to assign board seats and key staff and to determine other rights.

- **Alleviate capital contribution difficulties**

The CJV's foreign partner can contribute or lease to the joint venture expensive Western technology and equipment, such as medical diagnos-

Cooperative Joint Venture Case Studies

The following cooperative joint venture (CJV) cases illustrate potentially useful strategies that may apply to companies in other industries.

Case 1: A Chinese Toll Road CJV

Typically, toll road projects in China involve construction and operation of roads that have been classified and approved for toll collection. The PRC government sees toll roads as a way to encourage foreign investment in the development of China's transportation infrastructure.

CJVs are almost always used for such investments because other investment structures cannot effectively address the financial risk to investors that contribute a large amount of cash. A CJV enables such investors to recoup their investment more quickly than other structures, since the parties can negotiate how and when profits are ultimately divided. Because toll roads are "build-operate-transfer" projects (the assets—the roads—will return to the government at the end of a project's life), foreign investors are concerned about how much time it will take to recoup the investment and focus on more than just the total investment return by the end of the project. Since the value of cash flows declines over time, most foreign investors measure investment returns by internal rate of return. Foreign investors typically negotiate to get more than a proportionate share of the cash relative to share capital in the early years. For example, a foreign investor could negotiate to receive up to 100 percent of the available cash for an initial period (perhaps the first 5 to 15 years). In the next 5 to 10 years, available cash could be split to match the parties' shareholding. In a final period, perhaps the last 5 to 10 years, the foreign party could receive a share in the available cash less than proportionate to its shareholding. All agreements and definition of rights should be carefully spelled out in the detailed CJV contract.

In many toll road CJVs, the foreign party owns the majority of share capital. Most toll road CJVs have two categories of investors: financial and local government affiliate. Financial investors may be foreign or local; for the sake of simplicity they are called "foreign investors" here. This side contributes most of the needed cash. The second category of partners, which usually includes a subsidiary of the local traffic bureau, contributes licenses, construction, and the workforce. This side, for simplicity's sake called "local investors" here, puts in assets but may also contribute cash.

In one example of a toll road CJV, a project included an expressway and a Class 2 road (a parallel or connecting road giving access to the expressway). Most of the cash was used to build the expressway, and a lesser portion was used to repair and upgrade the Class 2 road. The foreign party maintained management control by assigning 60 percent of board seats—matching its share capital. The foreign party appointed the general manager and the financial controller so that it would be on top of daily operations and in charge of the material fund flows. The CJV set up checks and balances to communicate among foreign parties, local parties, and authorities. The CJV, a legal person with limited liability, had a four-year construction period and has a 30-year life. The parties divide profits based on the schedule described above. All of this was written into the CJV contract.

In toll road projects, the CJV structure should not inhibit exit strategies. Some investors view toll road projects as being similar to a utility with a limited life. Others have a strategy to expand their projects by adding more roads and by focusing on projects within a region or on key city-to-city projects. Thus, a successful exit strategy in this sector has been to pool toll roads and package them into a holding company for listing on a public stock exchange.

—*Paul H. Folta*

Case 2: A Chinese Gold Mining CJV

Today China is the world's fourth-largest gold producer. Growth in China's gold industry was driven by domestic demand and heavy government investment in the sector from the 1980s to the mid-1990s. With the deregulation of China's mining laws, the nation's World Trade Organization (WTO) entry in December 2001, and the official opening of the Shanghai Gold Exchange in October 2002, many observers believe the risk for foreign investment in this sector has fallen. Although a foreign investor registered in China as a representative office, equity joint venture (EJV), CJV (including a nonlegal person CJV), or a wholly foreign-owned enterprise (WFOE) may apply for an exploration license, the vast majority of foreign investments in this sector have been through CJVs.

Foreign companies set up CJVs in mining for many reasons. CJVs help counter government restrictions and can allow foreign investors to seek attractive financial returns and management control in exchange for taking risk and contributing capital. A CJV's flexibility can also help investors survive the high risk of failure in an individual mine because the partners can sign new contracts for new mines.

Companies also form CJVs in mining because no one can predict what will be extracted and because it is difficult to determine the value of an exploration and mining permit or mineral right—intangible assets that are usually owned by the state. Furthermore, intangible assets generally may not represent more than 35 percent of a project's registered capital. For potentially ore-rich areas, this might not grant enough shares for Chinese parties that do not wish to put up capital. Even though valuation methodologies for prospective mines exist, valuation could make the investment cost too high for foreigners who contribute most of the capital, want a significant return for their risk, and seek majority control of the project. The joint venture's Chinese partner is responsible for preventing the loss of state assets. If the exploration venture fails, rendering the exploration permit worthless, the foreign investor likely will return the exploration permit to the original Chinese owner so that there is no "loss of state assets" on paper. This is another reason why Chinese partners prefer the CJV structure.

In one example of a gold mining CJV, Victor Mining Ltd., a wholly owned subsidiary of SKN Resources Ltd. (SKN) of Canada, formed a CJV with a subsidiary company of the Henan Provincial Governmental Geological Bureau (HPGGB) in April 2004, to acquire a 70 percent effective equity interest in a high-grade silver and gold project in Henan. After initial exploration and contract revision, the contract was modified in summer 2004 to give SKN the right to acquire 77.5 percent of the silver and gold project. SKN will earn its stake by funding exploration and development and making cash payments over four years, with a first year minimum contribution of $750,000. HPGGB has a 22.5 percent

While the CJV is often more time-consuming and complex to negotiate in the beginning, it is this complexity that is its main benefit.

Case 3: A "Smart Card" Wireless Security Technology CJV

E-Smart Technologies, Inc., a US company with wireless security technology for smart cards, signed a CJV agreement with two Chinese companies in early 2004. Under the agreement, the CJV would operate nationwide value-added networks made up of e-Smart's operating platform and its multi-application, secure ID and payment smart cards; market the system and technologies to the government and financial sectors; and maximize the technology's use in as many fields as possible.

One of the Chinese CJV partners is majority owned and controlled by an entity of the Ministry of Information Industry (MII); the other is made up of Chinese media and public relations personnel. E-Smart owns half of this joint venture (the maximum allowed by law for a value-added service venture), and the two PRC companies will own 30 percent and 20 percent, respectively. E-Smart will contribute roughly $3 million in capital to the CJV over time, after all required permits and licenses are issued. This $3 million will represent 100 percent of the CJV's registered capital, though the venture may be expanded. E-Smart will own the exclusive licenses to provide and operate the system and technologies in China, and it will receive 20 percent of the CJV's gross operating income. The Chinese parties will use their relationships with the authorities to obtain the needed licenses and approvals, participate in market promotion and negotiations with customers, address network infrastructure issues, and help obtain financing. The board and operating management team will be determined by the parties in consultation with each other.

According to e-Smart executives, specific telecom sector restrictions had nothing to do with using the CJV structure (see p.22). "The CJV gave us the flexibility required to deal with the constantly changing circumstances, regulations, and laws one must contend with when doing business in China," they said. The CJV contract's flexibility allowed the company to negotiate with its prospective partners without having to argue about valuation methods. The CJV form also allowed e-Smart to obtain the management rights it desired, and the company's tax advisors felt more comfortable with the CJV for overall international tax planning.

The CJV required a detailed agreement (as, generally, would an EJV) and, coupled with all of the ancillary agreements and a clear licensing agreement, e-Smart believed that this detail helped protect its technology. According to a company spokesperson,

"All of the agreements mentioned made it very clear that the technology was not being transferred and that the ownership remained in our hands alone....While the CJV is often more time-consuming and complex to negotiate in the beginning, it is this complexity that is its main benefit. You are forced to think through all of the possible problems that may occur in the future and deal with them up front. The result is a smoother relationship with your partner(s) and a good blueprint for the operation of the CJV."

—Paul H. Folta

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interest based on its contribution of the mineral rights (exploration permits) covering the project. After SKN has earned its 77.5 percent interest, contributions to fund the exploration and development of the project will be made pro rata. The share capital of HPGGB, the Chinese property owner, may be diluted to no less than 10 percent if it elects not to make cash contributions.

An SKN representative explained that CJV structures are attractive for mining projects because the Chinese parties typically do not contribute working capital. To attract foreign investors, the Chinese side contributes the right to use, but not own, the property (all land in China is owned by the state). After 25 to 30 years the foreigners walk away.

An EJV structure is unsuitable in this sector because foreign investors usually require a share of the profit during that time period that is higher than their share of investment to compensate for their risk. Also, Chinese parties often seek a minimum carried interest. At the outset, it is unknown how much investment will be required to determine the prospects of a property. If the partners find nothing, then the joint venture must decide whether to invest in more exploration. Since further exploration could prove fruitless, the Chinese side typically would not want to invest cash to maintain its interest level. But if the mine is successful, then the Chinese side would want to be assured of a nondiluteable interest (such as the 10 percent carried interest in the silver and gold project). A CJV's flexibility can accommodate these divergent interests.

The CJV structure accommodates other contingencies as well. Often a mining project evolves in two stages. In the first stage the parties reach an agreement and form a CJV. The agreement usually contains a minimum expenditure requirement and an option to quit the project if the results are unsatisfactory and the expenditure requirement is met. But if the foreign investor quits, it will lose all rights (and liabilities).

China's foreign investment regulations require at least 15 percent of the project's registered capital to be contributed within three months after a business license is issued to the joint venture company governing the project. For example, if a project is given a $4 million total value, the Chinese side could contribute mineral rights negotiated at a value of $1 million for a 25 percent interest, and the foreign side could pledge to invest $3 million in cash for a 75 percent interest. The interest would be "earned-in" over an agreed period of time. In the second stage, the partners must decide—as exploration or mining proceeds—whether to make additional investments beyond the originally agreed amounts to achieve the project's goals. The Chinese and foreign parties may invest more at the same proportion, or one side can be diluted. Alternatively, the sides could agree to move the project to another property since many resources were invested to establish the company.

—Paul H. Folta

tic equipment. The CJV can then repay the foreign partner at an "advanced rate" from revenues before profit sharing. This strategy can be used in sectors in which the law caps foreign ownership and when the Chinese partner cannot afford to fund assets up front. Under an EJV ownership structure, such an arrangement is impractical or impossible unless the Chinese side can contribute the amount of cash or assets needed to fund its equity up to the minimum Chinese ownership level required.

■ **Allow more foreign management control**

Foreign partners can often obtain the desired level of control by negotiating management, voting, and staffing rights into a CJV's articles of association. Because these rights do not have to be allocated according to equity stakes, the CJV again provides more flexibility than an EJV.

■ **Reduce risk**

The CJV structure also tends to force partners to address rights and responsibilities in advance. The

The Ups and Downs of Telecom and Internet Joint Ventures

China's telecom and Internet sectors are slowly opening up to foreign direct investment, marking a shift from the uncertainty of and prohibitions against foreign investment in telecom projects in the 1990s.

In the early to mid-1990s, cooperative joint ventures (CJV) were the most common foreign investment structure in telecom. A format known as *Zhong-Zhong-Wai* (Chinese-Chinese-Foreign) was particularly popular. The Chinese partners in these projects were usually companies affiliated with China Unicom Ltd., a competitor to China Telecom, which was owned by the Ministry of Post and Telecommunications (MPT, now the Ministry of Information Industry [MII]). In these CJVs, the foreign parties often formed an offshore entity to lease equipment and provide consulting services through a CJV *(Zhong-Wai)* by using a revenue-sharing contract between the CJV's Chinese partner and the Chinese telecom operator, usually Unicom, *(Zhong-Zhong)*. The structure technically avoided equity "ownership" by the foreign party in a key asset—a license to access and operate services over the public switched network. The Chinese operator pledged use of the license to the CJV's Chinese partner. The CJV's Chinese partner thus acted in a role equivalent to a trustee. Throughout the 1990s, the legal status of such projects was at best uncertain. In the last half of the 1990s, China banned telecom joint ventures. Subsequently, a few Chinese telecom companies and their offshore investment vehicles successfully accessed capital through initial public offerings (IPOs). PRC rules that declared equity joint ventures (EJVs) the only form of foreign investment allowed in basic telecom and value-added services under China's WTO commitments took effect in January 2002.

The PRC government likely banned CJVs because they allowed foreign investors to negotiate disproportionate returns, management control, and protection of their technology when structuring deals with the financially weak Unicom. But after Unicom was placed under the powerful influence of MII, this was no longer a strong argument since, with more clout, Unicom and other Chinese telecom companies became better able to negotiate favorable terms for themselves.

Interestingly, in China's 2002 Catalogue Guiding Foreign Investment in Industry, telecom services were moved from the prohibited to the restricted category, and the catalogue does not specify the type of joint venture permitted. (As the *CBR* went to press in early December, China released another revision of the catalogue.)

Between 2002 and 2004, EJVs using "cooperative agreements" and a few CJVs were established, all providing Internet-related services. For example, AT&T Corp.'s "Unisiti" Shanghai Symphony Telecommunications EJV announcement in 2002 referred to "cooperation contracts" that were needed to access China's telecom network. (Though AT&T faced serious restrictions in equity, business scope, and geographic scope in the venture, AT&T and its Chinese partners have been able to achieve broader objectives through approved cooperative agreements.) In August 2004, American IDC Corp. and China Unioncom Digital Technology Co. formed an EJV with "cooperative contracts" to provide broadband Internet television technology to TV stations and other content providers across China. According to private equity investment groups that invested in or knew of other Internet projects, foreign investments in such projects in the past few years have structures similar to the *Zhong-Zhong-Wai* format, including one or more service agreements and equipment leasing arrangements. Some have been CJVs (see p.20).

Given the flexibility offered by separate commercial agreements that may accompany an EJV or CJV, the actual form of such joint ventures might not be of critical importance. Compared with IPOs, joint ventures can deliver more reliable funding to Chinese parties facing unpredictable stock markets and are not constrained by securities regulations designed to protect public shareholders. Arguably, CJV structures could provide greater comfort than EJVs to PRC authorities who might still be concerned about foreign direct equity ownership in traditionally sensitive "state assets," such as licensed carriers or software systems that access financial and personal data. Rather than complicate an EJV with too many side agreements, CJVs can offer more flexibility in foreign party financing, make it easier for foreign parties to recoup their investments, and give the foreign side the confidence—through practical mechanisms specified in the detailed CJV contract such as management controls—to contribute sensitive technology.

—Paul H. Folta

PRC government must approve all CJV investments to determine that the venture may legally engage in the specified business scope. Government approval of detailed CJV contracts has the added benefit of sanctioning the detailed agreements and deterring local partner noncompliance. Thus, CJV contracts commonly provide better recourse than EJV contracts if one partner fails to comply with agreements.

- **Are easier to terminate or modify**

Ending a CJV may be easier than ending an EJV—particularly if the partners held assets separately and clarified contingency dissolution terms in advance. In some sectors, when risk of failure in the development phase of a project is high, CJV contracts can be modified without terminating a partnership and forgoing investments and goodwill.

- **Resolve expense controversies**

If the CJV's foreign party finds it necessary to incur expenses that the Chinese party disapproves of, the expenses may be structured under a contract with the foreign party. For example, parties may be able to more easily resolve debates over the high cost of expatriates, whom the Chinese partner could consider unnecessary, by negotiating an acceptable cost in a service contract with the CJV.

- **Offer tax advantages**

Though CJVs and EJVs have the same tax advantages, CJVs offer some extra tax benefits. For instance, CJVs can sometimes appropriately avoid the asset transfer tax.

A CJV parties' profit, control, and risks are divided according to negotiated contract terms.

The future of CJVs

In a market economy with better laws and enforcement, the number of CJVs in China—in proportion to other investment vehicles—will continue to decline. But as long as SOEs and government entities want to do business, they will find ways to make EJVs and CJVs attractive investment options. Private Chinese entrepreneurs will increasingly see these vehicles only as temporary means to a different end—expansion without reliance on foreign equity partners. But since they too can benefit from foreign finance, technology, market access, and business know-how, some Chinese entrepreneurs may be willing to cut interesting and creative JV deals with foreign companies. 完

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WTO...

Julie Walton

Key commitments in services were to have been in place by December 11, 2004. What's next?

Four years into China's World Trade Organization (WTO) membership, most WTO members have moved past examining China's WTO participation strictly in terms of which commitments the country has implemented and which it has not. Rather, China's increasing integration into the global trading system has meant that members are responding more to China's active engagement on WTO issues, such as its market economy status and its dominance in textiles. In fact, the US-China Business Council's annual survey of its membership on China's WTO implementation indicates that China has become a key player in the global trading community (see p.26).

Service commitments in 2004: A mixed bag

In December 2003, China was somewhat behind in meeting its year-two service commitments, casting doubt on its ability to fulfill the range of far-reaching commitments that it had promised to meet in its third year of membership. Year four begins on a different note, reflecting China's good faith effort in 2004 in a number of contentious areas such as trading rights, distribution, and banking. In April 2004, the Ministry of Commerce (MOFCOM) issued a law and regulations that laid out the framework for opening trading and distribution rights to all foreign companies by the WTO deadline of December 11, 2004. MOFCOM also granted operational licenses to foreign companies to engage in nonbank auto finance and proceeded with required geographic phase-ins in banking and insurance on schedule. Furthermore, the China Insurance Regulatory Commission revised implementing rules governing foreign-invested financial organizations in July 2004, lowering minimum registered capital requirements and removing the restriction that only one new branch could be opened every 12 months.

Numerous concerns across a wide variety of sectors remain unaddressed, however. As the *CBR* went to press, MOFCOM had yet to release rules that would implement the distribution regulations allowing foreign investment in retail, wholesale, and warehousing. Another unresolved issue is whether companies will be required to establish independent subsidiaries to distribute products outside the scope of business defined in their existing business licenses. Nor have there been regulations detailing distribution procedures for pharmaceuticals, although the April regulations specified that these areas would be regulated separately.

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China made a good faith effort in 2004 in a number of contentious areas such as trading rights, distribution, and banking.

Capital requirements for insurance, banking, telecom, and construction remain prohibitively high, even though they were lowered for insurance and banking. Draft regulations for direct selling indicate that China plans to use high capitalization and other prudential requirements, such as years of experience in a given industry, to keep out all but the largest players. In express delivery, draft amendments to the PRC Postal Law would once again restrict the type of packages express delivery operators are allowed to carry. And in construction, residency requirements for foreign personnel, among other requirements, roll back most gains that were accorded in 2002 regulations that allowed wholly foreign-owned construction entities.

China's 2005 service commitments

The range and scope of China's service commitments that must be in place by December 11, 2005 are smaller than in previous years. The most notable change will be in the large number of sectors that will allow foreign investment in wholly foreign-owned enterprises (WFOEs). Change is already apparent in some sectors opened under the mainland's Closer Economic Partnership Arrangement (CEPA) with Hong Kong.

- **Advertising** WFOEs are to be permitted on December 11, 2005, although Star TV, the Hong Kong-based broadcast company, received MOFCOM approval in July 2004 to establish a wholly foreign-owned advertising company to sell advertising for the channels it currently broadcasts into China. Star TV qualified to establish the WFOE early through CEPA. The Shanghai Administration of Industry and Commerce approved Dow Jones Advertising (Shanghai) Co. Ltd. as China's first wholly foreign-owned advertising company for print media. This approval also came under CEPA.
- **Banking** Foreign companies are to be able to provide renminbi (RMB) services in four more cities by December 11, 2005: Ningbo, Zhejiang; Shantou, Guangdong; Shenyang, Liaoning; and Xi'an, Shaanxi. In early December 2004, China opened not only the three cities scheduled to open by December 11, 2004 (Beijing; Kunming, Yunnan; and Xiamen, Fujian), but also Shenyang and Xi'an, bringing the total number of cities open to RMB services to 18.
- **Insurance** Foreign companies will no longer be required to cede to China Reinsurance Corp. a portion of the lines of the primary risk for nonlife, personal accident, and health insurance. Furthermore, the minimum required total asset level to obtain an insurance brokerage license will fall to $200 million from a high of $500 million at accession.
- **Other** Foreign companies are to be able to establish WFOEs in courier services, freight forwarding, hotels, restaurants, and technical testing and analysis by December 11, 2005.

Trade in goods

China's average import tariff rate was to drop by less than 1 percent to 9.4 percent on January 1, 2005. Tariffs on information technology products, such as computers, semiconductors, and telecom equipment, were to drop to zero from an average of 13.3 percent.

Remaining quotas, except agricultural products under tariff-rate quota (TRQ) management, were also to be eliminated. This means that auto makers and their suppliers should no longer be subject to quota restrictions on the value of the products they import.

In agriculture, TRQ amounts for palm, rapeseed, and soybean oil were to rise 17.3 percent, 10.3 percent, and 15 percent, respectively, on January 1, 2005, when they were to have reached their final quota rate.

Textile troubles

The 30-year-old Multifiber Arrangement (MFA), which allocated export quota amounts to textile-producing countries, expired on December 31, 2004. This agreement prevented any single country from becoming a dominant

force in the global textile and clothing trade in part by allocating quota to small, less-developed economies. Nevertheless, China has emerged as a market leader, currently accounting for 20 percent of global textile trade. Some analysts predict this share could rise as high as 50 percent in 2005 after the quotas are lifted.

Several members have already taken their concerns over China's future dominance in textile trade to the WTO, hoping to come up with recommendations that address the problems that could arise as industry relocates to China. In October, China's WTO delegation blocked efforts to establish a formal working group to address the concerns of smaller economies that produce textiles and clothing. These petitioners have said they will continue to raise the issue throughout 2005 in the hope that once China's impact on the global textile trade is fully felt, more countries will want WTO assistance to address the situation.

As part of its WTO entry package, China agreed to provisions that could restrict its trade in textiles and clothing. If a WTO member believes that increased textile imports from China are causing market disruption, the member can request consultations with China to limit imports and impose a year-long, 7.5 percent cap on the growth of imports from China. This China-specific textile safeguard is in effect until December 31, 2008.

Most trade analysts believe that China could face a flood of safeguard cases against its textile and clothing exports. Cases emerged in the United States in

USCBC Member Priorities: WTO Survey Results

The US-China Business Council (USCBC) in July and August 2004 conducted a survey of member company views on China's implementation of its World Trade Organization (WTO) commitments. The survey results were used in the preparation of USCBC's report to the Office of the US Trade Representative in September 2004 on China's WTO implementation progress during its third year of membership.

Overall assessment

On a scale of 1 (excellent) to 10 (failure), USCBC members gave China an average (unweighted) performance score of 5.0. This represents a modest improvement over last year's score of 5.2. Ninety-two percent of respondents gave China a score between 3 and 7, with more firms reporting above average than below average progress.

Profile of respondents

Thirty-five percent of the Council's 231 members responded to the survey. Of those responding, 92 percent said that their business is affected by WTO implementation and 80 percent said it is significantly affected. Of the respondents, 95 percent were at the managerial level or higher, and nearly half were in manufacturing.

A number of member firms declined to respond to the 2004 questionnaire, indicating that questions of WTO compliance are declining in importance as China continues to evolve in the direction of a "normal" business environment. Furthermore, 19 percent of the companies that did participate provided only partial responses, explicitly stating that the WTO either does not directly address the concerns of their industry or that their company already has operational "workarounds" in place in areas of interest.

USCBC Members' Views of China's Progress Under WTO

Source: The US-China Business Council

Table 1: USCBC Members' Priority Issues

Issue	Weighted Score	Year 3 Rank	Year 2 Rank
Distribution Rights (ability to distribute product to wholesalers, retailers, and endusers within China)	120	1	3
Intellectual Property Rights (IPR): Enforcement	96	2	5
Trading Rights (ability to import and export product)	95	3	1
Nontariff Measures (quotas, licenses, tendering requirements)	89	4	6
IPR: Legal Framework	87	5	10 (tie)
Transparency	77	6	2
Specific Market Access Service Commitments	71	7	8
Standards, Technical Regulations & Conformity Assessment	60	8	4
Taxation	55	9	12
Customs & Trade Administration (classification, valuation, rules of origin)	49	10	10 (tie)
Nondiscrimination/National Treatment	47	11	9

Source: The US-China Business Council

late 2004, even before the MFA expired. The US Department of Commerce's Committee for the Implementation of Textile Agreements (CITA) in October and November agreed to investigate imports of socks and seven other textile products from China.

Lobbying for market economy status

China has indicated that it plans to use WTO rules to further its own trade and economic goals. For example, since 2003, senior PRC officials have made concerted efforts to have other WTO members change the way they treat China's economy for purposes of evaluating trade disputes, particularly dumping (selling goods overseas at prices below the cost of production at home). According to China's WTO entry documents, China will hold nonmarket economy status until December 11, 2016. China's nonmarket economy status means that economies that undertake dumping investigations against PRC companies can use third-country price data in place of Chinese data to determine whether dumping has occurred. The Chinese contend that this puts PRC domestic companies at an unfair disadvantage when fighting dumping allegations. China is subject to more dumping investigations than any other economy. Between 1995 and the end of 2003, China accounted for one-seventh of all dumping investigations initiated worldwide.

Continued on page 34

A number of member firms declined to respond to the 2004 questionnaire, indicating that questions of WTO compliance are declining in importance as China continues to evolve in the direction of a "normal" business environment.

Table 2: Effect of WTO Entry on USCBC Members' Top Business Issues

			WTO Impact on Issue (%)				
Rank	Weighted Score	Issue	Help	No Change	Harm	Unclear	No Opinion
1	125	Market Demand/Competition	**53**	22	6	13	6
2	117	Intellectual Property	**77**	10	0	8	5
3	108	Distribution/Logistics	**74**	10	3	3	10
4	103	Legal Infrastructure	**70**	13	0	10	7
5	88	Trade/Customs	**59**	10	3	14	14
6	77	Human Resources	29	**43**	10	5	14
7	72	Standards	**61**	26	4	0	9
8	71	Performance/Return on Investment	**45**	27	5	14	9
9	69	Investment Policies	**63**	21	8	4	4
10	59	Tax	26	**37**	11	16	11
11	53	Investment Structuring	**45**	14	9	18	14
12	52	US Visa Policies	5	**52**	19	10	14
13	42	Finance/Foreign Exchange	**44**	22	0	22	11
14	30	Political Risk	**60**	0	0	10	30
15	26	US Export Controls	11	**33**	**33**	11	11
16	21	Currency Value	14	**29**	0	**29**	**29**

Note: Bold numbers indicate the category with the highest percentage

Source: The US-China Business Council

Responses were roughly evenly split geographically, with nearly 51 percent of complete questionnaires coming from the United States, 49 percent from China (including Hong Kong), and less than 1 percent from elsewhere in Asia.

Top WTO-related issues

The USCBC asked each member company to select five priority issues from a list of 23 choices. Responding firms identified 11 issues as the most important (see Table 1). The issues were given a weighted score to reflect their relative importance to respondents. The score was calculated according to the number priority indicated by each firm using the following scale: Priority 1=5 points; Priority 2=4 points; Priority 3=3 points; Priority 4=2 points; Priority 5=1 point. Though few respondents thought issues had been satisfactorily resolved, most saw progress in each issue (see Figure).

Primary obstacles to implementation

The most commonly cited obstacles to China's implementation of its WTO commitments in the priority areas identified in the 2004 survey were government protectionism (central and local) and industry protectionism. The most notable exceptions to this pattern were in intellectual property rights (enforcement and legal framework), where lack of PRC resources and low level of understanding were named as the main obstacles, and in customs and trade administration, where respondents highlighted bureaucratic infighting and low levels of understanding.

Top business issues in China

Not every business issue in China is WTO-related, however. The survey also asked respondents to rank their companies' most important general business issues in China and the effect China's WTO entry has had on these issues. Market demand/competition, intellectual property, and distribution/logistics topped the list (see Table 2).

—US-China Business Council staff

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China's Bond Market Matures, Slowly

Government bonds still dominate the market

Chen Ji and Stephen Thomas

China's success in developing a fully functioning capital market depends in large part on whether it succeeds in establishing a thriving market for bonds. The government has, until recently, restricted the types of bonds that can be issued in China. But China's leaders have realized that there are powerful financial reasons to promote the expansion and deepening of the Chinese bond market. Among the most important are, first, that bonds would be desirable additions to the portfolios of Chinese insurance companies, banks, pension funds, and the country's social security fund, and second, that bonds are preferred investments for international investors. The bond market is also where China's growing business sector could raise long-term capital for expansion. A fully functioning bond market would also provide liquidity to China's rapidly expanding economy, not to mention its relatively young private housing and auto loan markets.

Chinese characteristics

China began selling Treasury bonds (T-bonds) in 1981, marking the launch of the first domestic bond market since 1949. The domestic bond market has since expanded significantly, both in terms of participants and financial functions. Bonds have been underwritten for two major groups: PRC government bodies (usually for the central government in the form of T-bonds issued by the Ministry of Finance [MOF]) and selected Chinese enterprises. Domestic bond issues have been medium to long term (3 to 20 years). China now has almost enough bond issues to establish interest benchmarks, but interest rates are still under the control of central government economic planning bodies. All central government (sovereign) bonds are approved as part of a government capital allocation plan based on a quota set each year by the State Council. Chinese bonds are also traded on a secondary bond market as part of the Shanghai and Shenzhen stock exchanges. Some interbank trading also occurs.

China's bond market today is a hybrid. In many ways, it functions like those in most developed and developing market economies. PRC government entities, financial institutions, and business enterprises all offer bonds; PRC government entities, financial institutions, and individuals may purchase bonds. Bond proceeds finance government deficits, government construction projects, financial institution liquidity requirements, and individual enterprise capital needs. The PRC government has also

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issued bonds in overseas markets denominated in US dollars, Japanese yen, and euros. Recently, the government approved short selling of bonds and instituted a bond index.

Yet the structures and practices of China's bond market also exhibit significant "Chinese characteristics." For example, because China's currency is not fully convertible for capital account transactions (that is, for capital-related, as opposed to trade-related, transactions), most foreigners may not buy Chinese bonds denominated in renminbi (RMB). The only exceptions are the nearly 30 foreign institutions in the recently created category of qualified foreign institutional investors (QFIIs). China also lacks a futures market for bonds because the government shut it down in the aftermath of a speculative frenzy in 1995.

So far, the government has approved only a few large, state-owned enterprises to issue corporate bonds. An annual government quota determines the amount of government and commercial bond issues, and corporate bonds make up about 5 percent of offerings. And finally, it is the government, not the market, that sets bond interest rates, although a market-determined yield curve is being established.

Bond varieties

■ Government bonds

Until 1995, China issued a number of different kinds of government and semi-government bonds (see the *CBR*, January–February 1998, p.30). State-owned investment banks issued semi-sovereign institutional domestic bonds for such groups as international trust and investment corporations (ITICs), but these were halted in 1995 after the Guangdong ITIC (GITIC), China's second-largest, failed. GITIC's foreign lenders were left with about 15 cents on the dollar (see the *CBR*, May–June 1999, p.36).

By 1995, the central government had consolidated bonds into four broad categories: two types of sovereign central government bonds, one for deficits and one for carrying out specific policies such as construction; overseas bonds issued by various governmental or government-approved groups; and corporate bonds, again requiring official examination and approval. MOF issues two kinds of sovereign bonds: 10- and 20-year T-bonds to finance China's annual government deficits, and 3- to 7-year bonds to support assorted Chinese construction and infrastructure projects. Together these two categories of bonds constitute about 95 percent of China's domestic bond market.

In 1994, the State Council ended MOF's Communist-era arrangement under which the ministry funded the government's deficit simply by drawing on the central bank. Consequently, the central government doubled its deficit between 1993 and 1994 from about ¥29.3 billion ($3.5 billion) to ¥57.4 billion ($6.9 billion) through sovereign bond issues. Since 1994, MOF has floated most of the national government bonds to finance China's yearly deficits, which result largely from China's relatively weak, but gradually improving, tax structure. The central government also has other financial responsibilities, such as funding social welfare programs. The share of national income used to pay interest on the national debt, though low, is also rising.

Foreign investors wishing to make a "China play" in bonds will find the Chinese bond market inhospitable, at least in the short term.

By 1997, the PRC government was issuing so many sovereign T-bonds to pay for its accumulating deficits and construction costs that together they accounted for 8.2 percent of GDP in 1997 alone.

The 1998 Asian financial crisis led to rising government expenditures and falling revenues. The resulting government deficit spending easily outpaced domestic GDP growth (see Table 1). To keep China's economy going through the crisis, Premier Zhu Rongji called for more long-term construction projects to help stoke domestic demand, thus starting a fiscal stimulus policy that lasted for several years.

Bonds Explained

A bond is a long-term (more than one year) loan with a legal obligation to repay the bond purchaser or lender the borrowed principal, as well as interest, at a future date. The length of loan, method of payment of interest, and interest rates are specific to each bond.

Once a bond is purchased, the purchaser or bondholder can sell the bond in a secondary market or own the bond until its date of maturity, when the borrower must repay the principal. The bond's value in a secondary market may vary with market interest rates and with changes in the credit rating of the issuer. Some bonds (convertible bonds) can be exchanged for stock if the bond issuer is a publicly traded company.

Sometimes the interest payments are built into the bond's initial offering price through reduction from the face value of the bond, called a zero-coupon bond.

Bonds can be offered by local governments (municipal bonds) or national governments (treasury or sovereign bonds). Proceeds from these types of bonds are used to meet long-term financial needs (for instance, US Treasury bonds finance the US deficit) or to fund long-term public projects, such as airports, highways, dams, bridges, and schools.

Bonds can also be offered by financial institutions or business enterprises (corporate bonds or debentures). Corporate bonds provide capital for business expansion.

—Chen Ji and Stephen Thomas

Table 1:
PRC Domestic Treasury Bonds for Deficit Financing, RMB billion

	Amount Issued	Cumulative Outstanding	
		Amount	% of GDP
1997	241.2	554.8	7.5
1998	380.9	776.6	9.9
1999	401.5	1,052.4	12.8
2000	465.7	1,367.4	15.3
2001	488.4	1,561.8	16.3
2002	593.4	1,933.6	18.9
2003	640.4	2,242.6	19.9

Source: Stephen Thomas and Chen Ji

Table 2:
PRC Domestic Treasury Bonds for Construction Projects, RMB billion

	Cumulative Outstanding	
	Amount	% of GDP
1997	349.1	4.7
1998	512.1	6.5
1999	644.7	7.8
2000	738.3	8.3
2001	853.4	8.9
2002	1,005.4	9.8
2003	1,019.4	9.0

Source: Stephen Thomas and Chen Ji

These projects were financed through the domestic bond market. From 1998 to 2002, China borrowed ¥660 billion ($79.8 billion) in long-term T-bonds to invest in about 10,000 projects in agriculture, water conservation, communication infrastructure, and technological upgrades (see Table 2 and the *CBR*, September–October 1999, p.16). The combined costs of these two rising expenses—deficits from the government balance sheet and construction bonds—were equal to 28.9 percent of GDP by 2003.

PRC National Development and Reform Commission Minister Ma Kai recently noted that because the economic situation has improved since 2003, the government was able to issue fewer construction T-bonds in 2004. He also pointed out that with the heavy use of T-bonds since 1998, China's economic growth has come to depend too heavily on government bonds, and alternatives need to be found.

■ **Corporate bonds**

Corporate bonds are popular in Western countries that have strong legal and credit rating systems. The corporate bond market is valued at about 140 percent of the GDP of the United States, about 95 percent of Japan's GDP, and about 85 percent of the European Union's GDP. China's low figure of less than 1 percent in 2003 is, however, comparable to most other East Asian countries except South Korea and Japan (see Table 3).

China's first post-1949 corporate bond was issued in 1987. By 2002, commercial enterprises, mostly large SOEs handpicked by the government and listed on China's stock exchanges, had issued about ¥270 billion ($32.7 billion) in bonds. By June 2003, 324 corporate bonds had been traded on the two exchanges. Twenty corporate bonds were still being traded in 2003, with a combined market value of about ¥45 billion ($5.4 billion), making corporate bonds about 5 percent of the total domestic bond market and less than 1 percent of China's GDP. China Mobile Communications Corp. (China Mobile), for example, issued bonds worth ¥5 billion ($604.9 million) in 2001. Although corporate bonds are usually issued to finance particular projects, China Mobile planned to use the proceeds of its bond issue to retire bank loans.

The relatively small size and slow growth of China's corporate bond market may also be the result of factors peculiar to China. First, it is difficult for qualified Chinese enterprises to obtain the required government permission to issue corporate bonds. One possible reason for this is that the government does not want to crowd out its favored enterprises, such as China Mobile, or its own T-bonds and construction bonds, even though depositors have more than ¥11 trillion ($133.1 billion) in Chinese banks. A second problem is that there is not yet a bond-rating agency able to monitor company performance (see the *CBR*, November–December 2003, p.36). And Chinese companies' opaque accounting practices provide bondholders with insufficient information. Finally, China lacks a sound legal framework to deal with companies that renege on their bond obligations. As the ultimate owner of the bond-issuing companies, the government has a conflict of interest—it does not want bondholders to take legal action against the government if the mostly government-owned companies were to default on their bond repayment obligations.

Moreover, the enterprises themselves, even if they are approved for bond issuance, may prefer to raise funds through bank loans. These loans are from state-owned banks that have traditionally been lax about demanding repayment. Listing on the stock markets may also be preferable to bond issuance because the corporations do not have to pay interest or principal on the money they raise. This is also why some corporate bond issuers would prefer to sell bonds that allow bondholders to convert to stocks. Since none of these barriers is likely to fall anytime soon, the corporate bond market will probably remain small for the near future.

Recently, the government has discussed ways to encourage banks to lend to small and medium-sized enterprises, possibly setting them on the path taken by larger state-owned enterprises, which have progressed from taking out bank loans, to listing securities, to issuing bonds. Despite the great promise that corporate bonds may offer, it appears that Chinese corporations will remain in step with most other East Asian companies by not depending much on bonds, despite their many benefits.

Role of foreign investors

Foreign investors wishing to make a "China play" in bonds will find the Chinese bond market inhos-

pitable, at least in the short term. First, the government is apparently ambivalent about the economic benefits of foreign investors' participation, either in selling or buying bonds. A number of advisors to the PRC authorities have pointed out the benefits of foreign involvement in the Chinese bond market, such as better corporate governance, but foreign investors have so far been unable to participate, except as QFIIs. The International Finance Corp., the private sector investment arm of the World Bank, and other multilateral institutions including the Asian Development Bank, hope to be able to float RMB bonds in China soon and use the proceeds to make development loans and support various development projects in China. A few foreign banks, after receiving permission to do business in local currency in China, would benefit from the ability to float RMB bonds. These bonds would provide the local currency reserves needed to make RMB loans, but the central government has yet to approve this proposed move.

One obvious impediment to foreign companies issuing bonds in RMB is the lack of RMB convertibility to foreign currency. The best bet for foreign financial institutions in the near future is to partner with Chinese domestic investment bankers to gain permission to jointly float RMB-denominated corporate bonds in China at the current low interest rates in order to build resources for lending in the Chinese market. Foreign banks may be able to gain permission for that kind of participation, but only within the state quota system that sets limits on the scope of foreign participation in the financial system.

Would-be foreign individual investors, for their part, may also be deterred by the lack of liquidity of Chinese bonds, although the secondary market in government bonds is active in Shanghai and Shenzhen. Potential foreign individual investors, then, will likely follow a "wait and see" strategy.

Table 3: PRC Domestic Corporate Bonds, RMB billion

	Total Corporate Bonds Outstanding	% of GDP
1997	63.3	0.9
1998	67.7	0.9
1999	77.9	0.9
2000	86.2	0.9
2001	100.9	1.0
2002	133.4	1.3
2003*	174.0	<1

* Estimated

Source: Stephen Thomas and Chen Ji

The wait for maturity

China already has a significant bond market that serves the needs of the PRC government in two important ways: by financing a growing deficit and by providing long-term financing for much-needed infrastructure projects. The Chinese companies that can get government support to float corporate bonds, such as large SOEs, will probably still prefer Chinese bank loans and stock offerings for some time to come. Some PRC corporations, such as Sinopec or Baoshan Iron and Steel Co., Ltd., that have a proven ability and willingness to repay and that need loans to expand or develop in proven markets, or to pay back existing bank loans, will issue corporate bonds.

Chinese individual investors will probably stick with government bonds, in which they now make up the majority of investors, because of the safety and tax-free status of government-issued bonds and the scarcity of investment alternatives caused by an uncertain stock market, low and taxable bank interest rates, the RMB's lack of convertibility, and the lack of confidence in most Chinese companies.

As the Chinese regulatory and legal structures for bonds improve, enterprise regulations become more comprehensive, company activities and financial records become more transparent, and China's banking system more developed, Chinese investors currently holding vast amounts of savings may channel more investments into corporate bonds. The need for higher-paying pension instruments, for long-term and reliable investments for insurance companies, and the investment needs of personal retirement funds will also stimulate demand in the Chinese bond market.

Yet reforms will be gradual and will only take place if their promised results convince leaders that the reforms will benefit the country, rather than simply being consistent with international practice. Foreign participation in China's bond markets will have to meet a similar litmus test, although some foreign participation may be permitted on the general principle of keeping good relations with foreign businesses that have been patiently waiting to do business in China.

The development and current state of the Chinese bond market again demonstrate that China is capable of making important reforms to develop its economy and improve its competitiveness in the global market. But they also show that China will continue making reforms in a carefully controlled and gradual way to ensure that they will not lead to major problems for the government or costs to the Chinese people. Foreigners will continue to play important advisory roles in these reforms and will, eventually, benefit financially by providing services that are consistent with Chinese economic objectives. 完

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WTO: Year 4

Continued from page 27

Argentina, Benin, Brazil, Kyrgyzstan, New Zealand, Togo, and members of the Association of Southeast Asian Nations recognized China as a market economy in 2004. As the *CBR* went to press, PRC officials were pressuring South Korea to designate China as a market economy. Although PRC government officials have lobbied the European Union and the United States heavily to recognize China as a market economy, neither has agreed to do so. The United States said it wants to see a "substantial rollback" of government control of raw materials and certain economic sectors, as well as more government transparency, before it will consider China a market economy. The European Union reached a similar conclusion, citing the government's large role in managing the economy, poor corporate governance, a discriminatory legal environment, and a lack of adherence to market principles in the financial sector as proof that China is still a nonmarket economy. China will likely continue to push the issue until the 2016 deadline comes to pass.

The questions and comments submitted during the TRM indicate that China has yet to embrace fully some of the fundamental principles of WTO membership.

Transitional review mechanism: Questioning China

During the last four months of 2004, China participated in its third transitional review mechanism (TRM). The TRM is a tool that other WTO members can use to monitor China's implementation. This unique, China-specific mechanism resulted from the fact that China entered the WTO before having a complete legal and institutional trade framework in place. Each year in the lead-up to China's December 11 accession anniversary, WTO members review China's implementation record, submitting questions to and hearing testimony from China's WTO delegation.

The most recent TRM submissions show that questions on China's WTO implementation have become more specific, focusing on issues that, according to members, China had not addressed in earlier TRMs or through bilateral discussions. To date, most of the questions have come from the United States, and the 2004 TRM was no exception, although Japan and the European Union are also regular contributors.

Even though China has made strides in implementing many of its specific commitments in goods and services, the questions and comments submitted during the TRM indicate that China has yet to embrace fully some of the fundamental principles of WTO membership, such as transparency and national treatment. For example, the US delegation questioned why nine of the technical standards China notified the WTO about in 2004 were submitted after the standard had come into force in China. Japan asked for clarification about why the PRC General Administration of Customs and the State Administration of Quality Supervision, Inspection, and Quarantine use different catalogues to determine which products need the China Compulsory Certification mark.

As in past years, China's studied vagueness in response to detailed questions frustrated participants in this year's TRM. China continued to respond in an unclear, often defensive manner, refusing in some cases to answer questions that it claimed were irrelevant to the committee topic (such as questions related to the Foreign Trade Law). The PRC delegation also cited inadequate time to prepare as a reason for not answering questions, even though the European delegation tried to prevent this problem by submitting written questions to the PRC delegation six weeks before the committee meeting. Members explicitly stated that China's participation in the TRM was "rather disappointing," noting that China frequently did not provide written answers and that oral answers to detailed questions were too vague. Members highlighted China's lack of transparency in virtually every committee session.

A "normal" business environment?

As the list of China's remaining goods and service commitments dwindles, companies might wonder whether the business environment in China is coming to resemble those in Western countries. On one hand, the openings that permit WFOEs in previously restricted sectors such as hotels, freight forwarding, construction, convention services, packaging, and repair and maintenance, allow companies to maintain greater control over their investment decisions. On the other hand, trade barriers still exist. Lower tariff rates mean little if an opaque import licensing system prevents a company from getting its product through Customs, as is the case with imported soybeans. Thus, though China is in a better position to implement its year-four WTO commitments than it was to implement its year-three obligations, the country still has some way to go before most foreign company representatives will agree that operations in China are "business as usual." 完

ACQUISITIONS IN CHINA:
Closing the Deal

Continued from page 17

■ Withholding tax on capital gains: 10 percent, applicable to sellers of equity in existing FIEs;
■ Business tax on transferred property and intangible assets: 5 percent, applicable to sellers in an asset acquisition;
■ Deed tax on land and buildings: 3–5 percent, applicable to buyers in an asset acquisition;
■ Real estate capital gains tax: 30–60 percent, applicable to sellers on capital gains from the resale of granted land;
■ Value-added tax (VAT) on machinery and equipment: 2 percent, applicable to sellers on certain equipment.

Companies considering an acquisition must exercise particular care regarding contingent tax liabilities and the timing of tax payments. Taxes that have not been paid by the closing date are likely to be assessed to the new enterprise. In addition, there is no statute of limitations on unpaid tax liabilities, exposing the new enterprise to contingent liability for income tax and VAT obligations that the acquired enterprise has underpaid for years or even decades. This is especially relevant because most domestic enterprises keep separate sets of "management accounts" and "tax accounts." The local tax bureaus routinely negotiate tax settlements with SOEs that are financially weak. In virtually every acquisition, contingent tax liabilities must therefore be addressed in the valuation of the business and in contractual warranties.

Keep close to the government

Above all, companies should align their acquisitions with government policy and with local interests. The central government has clear objectives in permitting the sale of domestic enterprises to foreign investors:
■ Transformation of existing SOEs into healthy enterprises that create employment, pay taxes, and support the local economy;
■ Introduction of "advanced foreign technology and management" into weak sectors and industries;
■ Use of foreign capital to help transform economically lagging Chinese regions like the Northeast and the West;
■ Modernization of the financial sector and public equity markets; and
■ The increased use of private capital to support further economic growth and to extend China's global reach.

Local interests vary but center on local economic development, job creation, and a stronger tax base. Companies that succeed in acquiring and restructuring local companies in China focused their efforts on government relations at each relevant level. The Kodak acquisition of controlling interests in four domestic film companies, even in the face of antitrust criticism in the local media, is a case in point.

The effort to build strong government relations should start early and continue through the acquisition process, formal government approvals, and post-acquisition restructuring. Positive chemistry and regular communication with the local government during the target identification and contract negotiation process lead to faster government approvals. Strong local government support during the approval phase makes it more likely that post-acquisition restructuring problems will be resolved quickly.

A formula for success

Acquiring a domestic company in China is not a game for the uninitiated or the faint of heart. The stakes are large and risks are evident at every turn.

The successful acquiring company must allocate substantial internal resources to planning and executing each step in the acquisition process. Project planning should include
■ **Establishment of a strong acquisition project team** at the outset, which includes both internal and external professionals with substantial China experience, not just long-term company insiders;
■ **Careful screening and selection of acquisition targets** based on defined strategic objectives, not on existing business partnerships or government introductions;
■ **In-depth financial, legal, market, operating, technical, and environmental due diligence** on the target company, with a focus on hidden and contingent liabilities and on the actual ownership of both fixed assets and intangibles, such as distribution systems, patents, copyrights, and trademarks;
■ **Valuation of the business** that fully reflects contingent liabilities and post-acquisition restructuring costs;
■ **Development of an employment restructuring plan** that is acceptable to the local community but that also provides for greatly increased labor productivity over time;
■ **Creation of post-acquisition milestones and performance-based incentives** for local management and key personnel that give them a personal stake in success and that help to identify and weed out poor performers.

Allocation of sufficient resources and achievement of these success factors will require the attention, hands-on involvement, and internal support of senior corporate executives throughout the acquisition process. 完

US Government Help on Foreign Bids

The Department of Commerce's Advocacy and Multilateral Development Bank Center, founded in 1993, aims to promote US exports, create and retain US jobs by supporting US companies' bids for international projects, and expand US businesses' global market share. The center concentrates on trade transactions—not policy.

An action center

The center uses US government resources to resolve unfair treatment of US firms by foreign government decisionmakers, politicized procurement processes, tenders tied up in a country's bureaucratic red tape, and problems that arise when foreign competitors receive assistance from their home countries' governments. The center assists US companies by coordinating advocacy by high-ranking US government officials through letters, phone calls, meetings with foreign officials, and trade missions. The center also conducts due diligence on companies, bids, and projects; determines whether a bid is in the US national interest; helps companies devise strategies; and acts as lead coordinator for US government commercial advocacy within the Trade Promotion Coordinating Committee (TPCC)—an interagency committee chaired by the secretary of Commerce. In exchange for these services, the center expects clients to maximize the US content of their exports.

Interview with Daniel J. Bloom

Daniel J. Bloom, executive director of the Advocacy and Multilateral Development Bank Center, recently discussed key elements of the center with Paula M. Miller, assistant editor of the *CBR*.

Q: How many cases for projects in China is the center currently handling? What sectors are most popular?

A: Currently, the center is tracking several dozen projects in China, with a total value of more than $30 billion. The most popular sectors are—by number of cases—aerospace, infrastructure/transportation, heavy machinery, energy and power, oil and gas, environment, and telecommunications.

Q: By the center's calculations, in 2004, how many US jobs may have been created through the center's assistance with China projects?

A: By our estimates, in 2004, China contracts won with our center's assistance created or retained roughly 30,000 US jobs.

Q: The center seems to emphasize helping small and medium-sized enterprises (SMEs). Does the center handle SME applications differently from those of large corporations?

A: We consider working with SMEs a high priority and recently created the position of a full-time, small business liaison—now filled by Joseph Enright—to conduct outreach to the SME community. Since June 2002, the center's staff has advocated successfully for about 36 contracts involving SMEs in China.

All requests, regardless of size, are reviewed in the same manner: Following the receipt of an advocacy request, the center conducts due diligence on the requesting company, the bid, and the project and then makes a national interest determination. After completing due diligence, the center's regional manager works with bidding companies and the US Commercial Service to devise an advocacy strategy that will craft an appropriate message to the foreign government, pinpoint the most effective medium for the message, and implement the advocacy strategy.

Q: How easy or difficult is it for US companies to win bids in China, compared to other countries? What are the biggest tender hurdles in China? How does the center help US companies overcome these hurdles?

A: China is one of the more difficult markets for US companies. The firms that are successful in China tend to develop a long-term commitment to the country. They know the market and the competition, and often have representative offices and good agents on the ground, developing long-term relationships that allow them to present the most competitive bids. They also have good exit strategies, should things go wrong.

China's unique legal and regulatory regime forces creative business alternatives. The PRC central government can override local rules, and recently promulgated national rules are sometimes applied retroactively. Chinese buyers often ask bidders to set up local manufacturing facilities, to be willing to transfer technology (it is wise to check with DOC's Bureau of Industry and Security—www.bxa.doc.gov—regarding possible technology transfer considerations), to bring subsidized financing, or to work with a Chinese partner.

Q: What is the center's relationship to export assistance agencies such as the US Export-Import Bank (Ex-Im Bank)?

A: The center works closely with these agencies and in recent years has signed memoranda of understanding (MOUs) with both Ex-Im Bank and the Private Export Funding Corp. (PEFCO). The MOU with Ex-Im Bank simplified and expanded access to financing programs for US exporters, including SMEs seeking US government advocacy assistance. The MOU with PEFCO capitalizes on PEFCO's relationship with the Ex-Im Bank and makes US dollar loans available to foreign importers that purchase goods and services of US manufacture or origin.

Recently, the center began managing commercial liaison efforts with multilateral development banks, including the

A US government agency helps level the playing field for American companies

Financial assistance

To serve its clients more effectively, the center has established relationships with US export assistance agencies such as the Export-Import Bank (Ex-Im Bank), the US Trade and Development Agency, and the Private Export Funding Corp. US company bids that already have financing lined up are more attractive to foreign decisionmakers.

Team China

In 2003, the Advocacy Center launched "Team China," which operates under the center's director, Daniel J. Bloom (see below). At present, the team consists of two regional managers for China—Roza Pace (roza.pace@mail.doc.gov) and Xiaobing Feng (xiaobing.feng@mail.doc.gov)—who work in Washington. Sean King is a special assistant for China under Neal Burnham, deputy assistant secretary in the US Commercial Service's Office of Domestic Operations. The Washington team interacts daily with Bruce Blakeman, special counsel to the secretary of Commerce, who is stationed with the Commercial Service in Beijing. The team focuses on US company requests for advocacy for specific export opportunities in China.

—China Business Review *staff and Advocacy and Multilateral Development Bank Center staff*

World Bank and the Asian Development Bank. Projects financed by multilateral development banks represent multibillion dollar commercial opportunities for US companies.

Q: How can projects qualify for center support? What are the minimum requirements?

A: The eligibility requirements for US government advocacy support are spelled out in the center's guidelines, which place a premium on US export content, including employment, in the determination of whether and to what extent a given bid is considered to be in the US national interest. Of course, there is no minimum transaction size for advocacy eligibility. The guidelines are posted on the center's website (www.export.gov/advocacy).

Q: What is a good example of a China case success?

A: In the summer of 2004, Landrum and Brown, Inc. (L&B), a small Ohio architectural firm, came to the center seeking US government advice and assistance on a bid for the design for the expansion of the Beijing Capital International Airport for the 2008 Olympics. The center helped L&B to secure a competitive financial package and to demonstrate the full support of the US government for this small business that was new to the China market. Specifically, the center helped L&B acquire a letter of interest from the Ex-Im Bank, which was then submitted for an expedited review procedure under the MOU between the bank and the center. In addition, the center worked with the Trade and Development Agency to help the company secure a training grant, contingent upon L&B winning the tender.

The center also developed an advocacy strategy aimed at leveling the playing field to offset high-level advocacy support received by L&B's competitors. (L&B's foreign competitors received foreign-government advocacy assistance at the ministerial and prime-ministerial levels.) As the runner-up in the Beijing competition, the firm received a monetary award, which it used to compete on another project in China.

Soon after winning second place in the Beijing competition, L&B was invited to bid for the design for the expansion of the Shanghai Pudong Airport. This time the company was awarded first place. In winning the Shanghai contract, the Cincinnati company, with fewer than 100 employees, beat out large multinational players from around the globe. The center was recently informed that things are going well for L&B in Shanghai and that the process has been a huge success. The company believes that US government support improved its business prospects in China where numerous project expansions are planned over the next decade.

Q: What are your top three suggestions for US companies hoping to export to China?

A: Know your market, know your customer, and know how you want to get paid. That means sell products that China needs, enter sales contracts with solvent partners, and pay attention to how, when, and in what currency you will get paid. Make sure you are in compliance with US and PRC trade laws. Become familiar with the Foreign Corrupt Practices Act and make sure that your product does not require a US export license. Make sure that the product meets Chinese standards, which may differ from US standards.

If a company is already an exporter and is looking to expand into the China market, this is a good place to start:

- Visit the China Business Information Center's (BIC) website (www.export.gov/china) or call 800-872-8723. BIC offers clients access to counseling with trade specialists in the United States and referrals to US Commercial Service officers in China and helps channel trade leads to clients through US Export Assistance Centers (USEAC) located throughout the United States.
- Meet with your state USEAC representative to discuss your specific needs. You can find the appropriate USEAC by calling the BIC phone number listed above.
- Talk to your local state office that deals with trade issues.
- Join organizations such as the US-China Business Council [www.uschina.org; publisher of the *CBR*], or state China business councils to network with people with similar interests, educate yourself on how to do business in China, and meet PRC and US government officials working on China trade issues.

Opportunities

News of China-related educational, cultural, and charitable projects

Opportunities introduces significant charitable, cultural, and educational projects that seek American business support and aims to help companies identify programs that merit their assistance. The materials contained in *Opportunities* are boiled down; our goal is to provide contact information and only the most skeletal description of each organization's interests. We strongly encourage interested companies to contact the programs contained here directly, so that each firm can review the more-detailed materials that individual organizations can provide.

American companies participate in a broad range of programs that bring benefit to the people of China and strengthen the bonds of US-China friendship beyond the commercial realm. *Opportunities* is intended to help companies explore new ways of making a difference.

(Note: Neither the US-China Business Council nor the *CBR* is a sponsor of any project listed in *Opportunities* and makes no recommendation with regard to corporate assistance to any specific project.)

US Institution: **Girls Global Education Fund**
PRC Institution: **Guangxi Charity Association and local education departments**
Project Description: **Sponsor girls who would otherwise be unable to attend school.**

Girls Global Education Fund (GGEF), a 501(c)(3) nonprofit organization, was founded in 1996 to provide scholarships to girls in developing countries who would otherwise be unable to attend school. GGEF gives scholarships to girls in primary, junior high, and high school. GGEF covers the cost of sending girls to school for the entire year, and if necessary, also pays for transportation to school and lunch. To remain in our program, a student must complete the school year with satisfactory grades and attendance.

In 1997, GGEF launched its pilot program in Guangxi, China, sending 63 girls to school. To date, GGEF has sponsored more than 150 girls, all of whom completed the school year and returned for the next. GGEF also sponsors several college and vocational school students.

Contact Information: Robin Bernard, Executive Director
Girls Global Education Fund
PO Box 1002
Planetarium Station
New York, NY 10024-0547
Tel: 212-799-5703 E-mail: rbernard@ggef.org www.ggef.org

US Institution: **International Institute of Rural Reconstruction (IIRR)**
PRC Institutions: **Regional Development Research Center at Yunnan University (RDRC); Yimen County Government, Yimen County, Yunnan. Additional partner organizations may be selected as the program progresses.**
Project Description: **Build capacity in and mentor RDRC to create a training center in Yunnan aimed at enhancing the skills of partner organizations to work with local government officials and communities in rural development and to offer relevant short-term training courses.**

IIRR has more than 40 years of experience conducting international training courses in participatory rural development methodologies and is well placed to work with Chinese institutions in Southwest China. Research by these partner institutions has demonstrated a need to improve rural development practices in some of China's poorest, most remote regions through developing local-level officials' abilities—as well as their local community partners' abilities—to implement participatory, people-centered, and integrated rural development. The goal is for the Chinese partner institutions to work in communities and develop, and eventually conduct, training courses for county and township officials.

IIRR has conducted multiple training courses, study programs and field projects with PRC agencies and organizations in China, as well as at IIRR's campus in the Philippines. In September 2004, IIRR established an office in Kunming, Yunnan, China.

IIRR is currently seeking corporate scholarships and corporate and individual contributions for the China Program.

Contact information: Dr. Pratima Kale, President
International Institute of Rural Reconstruction
333 East 38th Street
New York, NY 10016
Tel: 212-880-9147 Fax: 212-880-9148 E-mail: nyc.office@iirr-us.org www.iirr.org

THE US-CHINA BUSINESS COUNCIL
FORECAST 2005

Forecast 2005
A members-only annual conference
Washington, DC

Reception: February 2, 6:00-8:30 pm

Conference: February 3, 8:30 am-2:15 pm

Chinese Politics and Policy Trends
Dr. Kenneth Lieberthal, Visiting Fellow in Foreign Policy Studies, The Brookings Institution; Distinguished Fellow and Director for China at the William Davidson Institute, William Davidson Professor of Business Administration, and Professor of Political Science, University of Michigan

China's Economy in 2005
Dr. Nicholas Lardy, Senior Fellow, Institute for International Economics

Preview of Bilateral Trade Issues in 2005
Mr. Charles Freeman, Assistant US Trade Representative (USTR) for the People's Republic of China, Taiwan, Hong Kong, Macao, and Mongolia (invited)

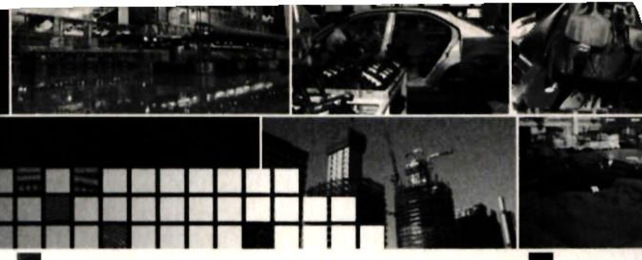
Projections for the Business Environment
Patrick Powers, Director, China Operations, The US-China Business Council

Luncheon Address:
US-China Trade Relations in 2005: The View from the Hill
Senator Max Baucus, Ranking Member, US Senate Finance Committee (invited)

Benchmarking Sessions
(Optional Afternoon Programs) (2:15-3:30 pm) on realizing trading and distribution rights and integrating China into global sourcing operations

Forecast 2005 will be held at the St. Regis Hotel, Washington, DC.
For more details, fees, lodging, and registration information, see ***www.uschina.org***

Contact: Gloria González-Micklin, Director of Programs, The US-China Business Council
Tel: 202-429-0340; ggonzalezmicklin@uschina.org



Sales and Investment September 16–November 15, 2004 Compiled by Doris Grage and John Kemmer

The following tables contain recent press reports of business contracts and negotiations exclusive of those listed in previous issues. For the most part, the accuracy of these reports is not independently confirmed by the CBR. Contracts denominated in foreign currencies are converted into US dollars at the most recent monthly rate quoted in the International Monetary Fund's International Financial Statistics.

Firms whose sales and other business arrangements with China do not normally appear in press reports may have them published in the CBR by sending the information to the attention of the editor.

Agriculture

INVESTMENTS IN CHINA

Penn Biotech Inc. (Canada)
Signed letter of intent with China's Ministry of Agriculture to form a joint venture to grow seed potatoes. 10/04.

Architecture, Construction & Engineering

INVESTMENTS IN CHINA

Morgan Stanley (US)/Ji'nan Shanshui Group Co. Ltd.
Formed cement production joint venture in Shandong. (US:30%-PRC:70%). $50 million. 10/04.

Automotive

INVESTMENTS IN CHINA

Mahindra and Mahindra Ltd. (India)/Jiangling Motor Co. Group (Jiangxi)
Signed MOU to form joint venture to acquire the tractor manufacturing assets of Jiangling Tractor Co., a subsidiary of Jiangling Motor Co. Group. (India:80%-PRC:20%). $10 million. 11/04.

Araco Corp., TakaNichi Co., Toyoda Boshoku Corp. (Japan)/Guangzhou Automobile Corp.
Formed joint venture, Guangzhou Intex Autoparts Co., to produce interior auto parts. $19 million. 10/04.

General Motors Corp. (US)/Shanghai Automotive Industry Corp. (Group)
Agreed to jointly develop and market hybrid and fuel-cell vehicles. 10/04.

Johnson Controls Inc. (US)/Dongfeng Motor Corp., Shanghai Automotive Industry Corp. (Group)
Formed vehicle-seat joint venture in Guangzhou. $4.1 million. 10/04.

Nachi-Fujikoshi Corp. (Japan)/Shanghai Automotive Industry Corp. (Group)
Formed joint venture, Nachi Shanghai Bearings Co. Ltd., to manufacture bearings for use in automotive air conditioning units. (Japan:67%-PRC:33%). $2.1 million. 10/04.

Continental AG (Germany)/Qingdao Doublestar Tire Industrial Co. Ltd.
Signed MOU to form joint venture, Continental Doublestar Co. Ltd., to produce automobile tires. 09/04.

Aviation/Aerospace

CHINA'S IMPORTS

Airbus SAS (France)
Won contract to supply eight A319 aircraft to Hainan Airlines. 11/04.

Eurocopter SA (France)
Sold two helicopters to CITIC Offshore Helicopter Co. Ltd. $24.7 million. 11/04.

Airbus SAS (France)
Won contract to supply 20 A330-300 aircraft to China Eastern Airlines. $3.3 billion. 10/04.

Airbus SAS (France)
Awarded contract to supply six A319 aircraft to Air China Ltd. 10/04.

The Boeing Co. (US)
Sold three Boeing 737-800 aircraft to Hainan Airlines. $200 million. 10/04.

Rolls-Royce plc (UK)
Won contract to supply Trent 700 engines to power 20 Airbus A330-300 twinjets for China Eastern Airlines. 10/04.

INVESTMENTS IN CHINA

Agusta Aerospace Corp., a subsidiary of Agusta Westland (UK)/Jiangxi Changhe Aviation Industries
Formed joint venture to produce, market, sell, and support the A109 Power helicopter. 11/04.

Abbreviations used throughout text: ABC: Agricultural Bank of China; ADB: Asian Development Bank; ASEAN: Association of Southeast Asian Nations; AVIC I and II: China Aviation Industry Corp. I and II; BOC: Bank of China; CAAC: General Administration of Civil Aviation of China; CATV: cable television; CBRC: China Banking Regulatory Commision; CCB: China Construction Bank; CCTV: China Central Television; CDB: China Development Bank; CDMA: code division multiple access; CEIEC: China National Electronics Import and Export Corp.; China Mobile: China Mobile Communications Corp.; China Netcom: China Netcom Corp. Ltd.; China Railcom: China Railway Communications Co., Ltd.; China Telecom: China Telecommunications Group Corp.; China Unicom: China United Telecommunications Corp.; CIRC: China Insurance Regulatory Commission; CITIC: China International Trust and Investment Corp.; CITS: China International Travel Service; CNOOC: China National Offshore Oil Corp.; CNPC: China National Petroleum & Gas Corp.; COFCO: China National Cereals, Oils, and Foodstuffs Import and Export Corp.; COSCO: China Ocean Shipping Co.; CSRC: China Securities Regulatory Commission; DSL: Digital Subscriber Line; ETDZ: economic and technological development zone; GSM: Global System for Mobile Communication; ICBC: Industrial and Commercial Bank of China; IT: information technology; LNG: liquified natural gas; MII: Ministry of Information Industry; MOFCOM: Ministry of Commerce; MOU: memorandum of understanding; NA: not available; NDRC: National Development and Reform Commission; NORINCO: China North Industries Corp.; PAS: personal access system; PBOC: People's Bank of China; PetroChina: PetroChina Co., Ltd.; R&D: research and development; RMB: renminbi; SARFT: State Administration of Radio, Film, and Television; SEZ: special economic zone; SINOPEC: China National Petrochemical Corp.; SINOTRANS: China National Foreign Trade Transportation Corp.; UNDP: United Nations Development Program; SME: small and medium-sized enterprise; WFOE: wholly foreign-owned enterprise

Airocean Group, A-Sonic Aerospace (Singapore), China Xpress Pte Ltd., a subsidiary of China Credit Holdings Ltd. (Hong Kong)/Guangdong Travel Service Holdings Ltd.

Formed joint venture to provide budget airline service throughout China. (Singapore:44%-Hong Kong:5%-PRC:51%). $10 million. 10/04.

Cathay Pacific Airways Ltd. (Hong Kong)

Agreed to purchase 9.9% of Beijing-based Air China Ltd. 10/04.

Singapore Technologies Aerospace, a division of Singapore Technologies Engineering/China Eastern Airlines Co., Ltd. (Shanghai)

Formed joint venture, Shanghai Technologies Aerospace Co., Ltd., to perform commercial aircraft maintenance, repair, and overhaul. (Singapore:49%-PRC:51%). $98 million. 10/04.

OTHER

FedEx Express, a unit of FedEx Corp. (US)

Won 12 additional weekly flights to China. 10/04.

NWA Cargo, the cargo subsidiary of Northwest Airlines (US)

Won six additional weekly flights to China. 10/04.

Polar Air Cargo, Inc. (US)

Will increase US-Shanghai flights from six to nine per week. 10/04.

SAS AB (Sweden)

Increased Shanghai-Copenhagen flights from three to six per week. 10/04.

Banking & Finance

CHINA'S IMPORTS

Financial Fusion, Inc., a subsidiary of Sybase Inc. (US)

Selected by BOC to provide online banking services throughout China. 10/04.

Reuters Group plc (UK)

Signed agreement to provide a real-time, Internet-based foreign exchange platform for the China Foreign Exchange Trade System, a PBOC subsidiary. 10/04.

OTHER

Baird Capital Partners (US)

Established representative office in Shanghai to support its US portfolio companies operating in China. 11/04.

Citigroup Inc. (US)

Purchased $121 billion in nonperforming loans from China Huarong Asset Management Co. 11/04.

Chemicals, Petrochemicals & Related Equipment

CHINA'S IMPORTS

Technip (France)

Won contracts to provide nine cracking furnaces and ethylene production technology to CNPC's petrochemical units in Jilin and Liaoning. 10/04.

INVESTMENTS IN CHINA

Lanxess (Germany)/Weifang Yaxing Chemical Corp. (Shandong)

Formed joint venture, Lanxess-Yaxing Chemical Corp., for production of aqueous hydrazine. (Germany:55%-PRC:45%). $23 million. 10/04.

Rhodia (France)/China National Blue Star Corp. (Beijing)

Agreed to form silicon production alliance in Tianjin. (France:25%-PRC-75%). 10/04.

Consulting

INVESTMENTS IN CHINA

Acxiom Corp. (US)

Acquired ChinaLOOP, a Shanghai-based business-intelligence, customer-relationship-management, and data-management company. 10/04.

Distribution, Logistics & Related Services

INVESTMENTS IN CHINA

Royal Vopak NV (the Netherlands)/COSCO (Beijing)

Formed joint venture to provide liquid chemical international freight management, domestic warehousing, and delivery management services. (the Netherlands:50%-PRC:50%). 11/04.

ComfortDelGro Corp. Ltd. (Singapore)/Shenyang Anyun Group Co. (Liaoning)

Formed joint venture, Shenyang ComfortDelGro Anyun Bus Co. Ltd., to run urban transport services, charter tour coaches, rent out advertising space on its buses and bus stops, and maintain and repair vehicles. (Singapore:80%-PRC:20%). $26 million. 09/04.

Electronics, Hardware & Software

CHINA'S IMPORTS

Citect Pty Ltd. (Australia)

Won contract from China Gas Co. Ltd. for a software system to control and monitor gas distribution to 5.5 million households in seven mainland cities. $2 million. 11/04.

NEC Corp. (Japan)

Received orders for digital TV transmitters from Shanghai Technology Development Co., Ltd. and Shanghai Oriental Pearl Transmission Co., Ltd. 10/04.

AsiaInfo Holdings, Inc. (US)

Won contract to implement phase III of its customer relationship management system for Sichuan Mobile Communication Co. 10/04.

INVESTMENTS IN CHINA

Gamma Projects (UK)/Datang CATTSoft, a unit of Datang Telecom Technology and Industry Group (Beijing)

Agreed to co-market their software products internationally. 10/04.

NAVTEQ Corp. (US)/China Navinfo Co., Ltd. (Beijing)

Formed joint venture, NAV2, to provide digital mapping solutions in China. 10/04.

OTHER

Red Hat, Inc. (US)

Opened office in Beijing to market Linux software and associated services. 11/04.

UbiNetics Ltd. (UK)

Opened a wireless R&D and support operation facility in Shenzhen. 11/04.

Lexar Media Inc. (US)/Digital China Holdings Ltd. (Beijing)
Entered into strategic distribution agreement for Digital China to distribute Lexar's complete line of flash memory cards and digital music players in China. 10/04.

SAP Aktiengesellschaft (Germany)
Opened a new SAP Global Support Center in Dalian, Liaoning. 09/04.

Energy & Electric Power

CHINA'S IMPORTS

ABB Ltd. (Switzerland)
Won contracts to supply a switchgear and 12 sets of power transformers to the Three Gorges Dam project. $60 million. 10/04.

ALSTOM (France)
Signed contract to provide power-generating equipment to Bailianhe Pumped-Storage Co., Ltd. in Hubei, Guangdong Pumped Storage Co., Ltd., and State Grid Henan Baoquan Pumped Storage Co., Ltd. 10/04.

ALSTOM (France)
Signed contract to transfer design and manufacturing technology of single-stage reversible pump-turbines and motor-generators to Harbin Electrical Machinery Co. Ltd. and Sichuan's Dongfang Electrical Machinery Co. Ltd. 10/04.

Emerson Process Management (US)
Won contract to install its IT control system in the Wangting Combined Cycle Power Plant. 10/04.

GE Energy, a division of General Electric Co. (US)
Won contract to supply four turbine-generator sets to the new Xixiayuan hydroelectric facility in Henan. $35 million. 10/04.

Siemens Power Generation Group, a unit of Siemens AG (Germany)
Will supply nine gas turbines to four power plants in China. $266 million. 10/04.

Siemens Power Generation Group, a unit of Siemens AG (German)
Received order from Shenzhen Fuhuade Electric Power Co., Ltd. to operate a gas turbine power plant for 10 years. $101 million. 09/04.

INVESTMENTS IN CHINA

CompAir Group (UK)/Shanghai Electric Co.
Formed joint venture to manufacture equipment used in compressed natural gas stations. (UK:60%-PRC:40%). $7 million. 09/04.

Environmental Equipment & Technology

CHINA'S IMPORTS

Suez SA (France)
Won water and waste treatment contracts for Qingdao and Shanghai Chemical Industrial Park, respectively. $845 million. 10/04.

Veolia Water, a division of Veolia Environnement SA (France)
Won contracts to renovate water treatment plants in Hohhot, Inner Mongolia, and Weinan, Shaanxi. $971 million. 10/04.

Golden Idea Bio-Engineering (Dongguan) Co., Ltd., a subsidiary of Bio-Treat Technology Ltd. (Singapore)
Won contract to construct drainage pipes in Kunshan, Jiangsu. $19 million. 09/04.

Golden Idea Bio-Engineering (Dongguan) Co., Ltd., a subsidiary of Bio-Treat Technology Ltd. (Singapore)
Won contract to provide waste-water treatment services and construct a new waste-water treatment plant in Kunshan, Jiangsu. $57 million. 09/04.

Golden Idea Bio-Engineering (Dongguan) Co., Ltd., a subsidiary of Bio-Treat Technology Ltd. (Singapore)
Won contract to provide waste-water services to a municipal waste-water treatment project in Dafeng, Jiangsu. $8.5 million. 09/04.

Seghers Keppel Technology Group (Belgium), a subsidiary of Keppel Corp. Ltd. (Singapore); China Everbright International Ltd. (Hong Kong)
Signed contract to provide engineering for the Suzhou Suneng Waste Incineration Power Plant. 09/04.

Seghers Keppel Technology Group (Belgium), a subsidiary of Keppel Corp. Ltd. (Singapore)
Won design contract for the waste and ash handling facility at the Suzhou Suneng Waste Incineration Power Plant. 09/04.

Food & Food Processing

INVESTMENTS IN CHINA

InBev (Belgium)
Acquired the remaining 45% of Hunan Debier Brewery Co. Ltd. 11/04.

Actis Capital LLP (UK)
Invested in Ningxia-based beverage producer and marketer, China Wolfberry Holding Co. $10 million. 09/04.

Carlsberg AS (Denmark)
Acquired 34.5% of Xinjiang-based Wusu Brewery. 09/04.

OTHER

Anheuser-Busch Cos., Inc. (US)/The International Olympic Committee/Beijing Organizing Committee for the Games of the XXIX Olympiad
Announced Budweiser will be the international beer sponsor of the 2008 Beijing Olympics. 09/04.

Insurance

INVESTMENTS IN CHINA

AEGON-CNOOC Life Insurance Co. Ltd., a joint venture between AEGON NV (the Netherlands) and CNOOC (Beijing)/ABC
Signed national cooperation agreement to provide life, accident, and health insurance services to ABC's customer base. 10/04.

OTHER

Aviva-COFCO, a joint venture between Aviva plc (UK) and COFCO (Beijing)
Opened new branches in Chengdu, Sichuan, and in Beijing. 09/04.

Light Industry/Manufacturing

INVESTMENTS IN CHINA

Pirelli & C. SpA (Italy)/Aeolus Tire Co., Ltd. (Henan)
Signed letter of intent to set up joint venture to produce truck radial tires in Henan. 11/04.

Toshiba Corp. (Japan)/TCL Corp. (Guangdong)
Will form joint venture to manufacture home appliances in China. (Japan:70%-PRC:30%). $13.6 million. 11/04.

OTHER

Rexam plc (UK)
Will acquire the remaining 40% of Rexam Beverage Can Zhao Qing from its joint venture partner, Hua Xing Investment Ltd. 11/04.

Machinery & Machine Tools

CHINA'S IMPORTS

MOS International plc (US)
Received order from CNOOC to provide two marine deck cranes for the Panyu/Huizhou gas development project. $1.9 million. 11/04.

CHINA'S INVESTMENTS ABROAD

FAG Kugelfischer AG (Germany)
Agreed to sell its 94.9% stake in sewing machine manufacturer Durkopp Adler AG to Shanghai's Shanggong (Group) Co., Ltd. $1.2 million. 10/04.

Media, Publishing & Entertainment

CHINA'S IMPORTS

HBO Asia, a subsidiary of Home Box Office, Inc. (US)
Signed agreement to broadcast three HBO movies a day on China Digital Television Production's First Cinema digital pay channel. 10/04.

INVESTMENTS IN CHINA

Warner Bros. Entertainment Inc., a subsidiary of Time Warner Inc. (US)/China Film Group, Hengdian Group (Zhejiang)
Formed joint venture, China Movie-Warner-Hengdian Movie Ltd., to produce and distribute Chinese-language feature films and TV programs. (US:30%-PRC:70%). 10/04.

Warner Bros. International Cinemas, a unit of Warner Bros. Entertainment Inc. (US)/Guangzhou Jin Yi Film and Television Investment Co. Ltd.
Formed joint venture for the construction of a multiplex theater in Beijing. 10/04.

Viacom Inc. (US)/Beijing Television
Formed partnership to produce Chinese-language music and entertainment programming for domestic and international distribution. 09/04.

OTHER

Television Broadcasts Ltd. (Hong Kong)
Won the right to broadcast in Guangdong. 09/04.

Medical Equipment & Devices

CHINA'S IMPORTS

Candela Corp. (US), Chindex International, Inc. (US)
Signed distribution agreement for Chindex to market Candela's line of aesthetic laser systems to healthcare providers. 10/04.

INVESTMENTS IN CHINA

Guangyi Expo Group Inc. (US)/Guangxi Guangyi Chinese Medical Herb Co. Ltd.
Formed joint venture, Guangxi Guangyi Medicine Co. Ltd., to produce and market traditional Chinese medicines. (US:51%-PRC:49%). $1.2 million. 11/04.

Guangyi Expo Group Inc. (US)/Guangxi Guangyi Chinese Medical Herb Co. Ltd.
Agreed to jointly build an international medicine exhibition center in Guangxi. $120 million. 11/04.

Metals, Minerals & Mining

CHINA'S EXPORTS

China Harbor Engineering Group (Beijing)
Signed contract with Fortescue Metals Group Ltd. to provide financing, design, and construction for large-scale works covering dredging, train unloading, ore stacking, blending, and ship loading facilities at Fortescue's selected export outlet in Port Hedland, Australia. $368 million. 11/04.

China Metallurgical Construction (Group) Corp. (Beijing)
Signed contract with Fortescue Metals Group Ltd. to provide financing, design, and construction for a mine and beneficiation plant at Christmas Creek, Australia. $321 million. 11/04.

CHINA'S IMPORTS

Fortescue Metals Group Ltd. (Australia)
Won 20-year contract to supply iron ore to Hebei Wenfeng Iron and Steel Co. Ltd. $950 million. 10/04.

Fortescue Metals Group Ltd. (Australia)
Won 20-year contract to supply iron ore to Jiangsu Fengli Group. 10/04.

Fagor Arrasate, a subsidiary of Mondragon Corporacion Cooperativa (Spain)
Received order from Chinese consortium FAW-Baosteel-Sumitomo to manufacture an automated cutting line with press for processing steel reels. $9 million. 09/04.

INVESTMENTS IN CHINA

Kobe Steel Ltd., Kyodo Shaft Co. Ltd., Metal One Corp., Sugita Wire Ltd. (Japan)
Will form joint venture, Kobe Wire Products (Foshan) Co., Ltd., to manufacture steel bars and wires for Japanese auto parts manufacturers in China. $6.7 million. 11/04

American Construction Co. (US)/China Inner Mongolia Baogang Steel Union
Agreed to form joint venture, Baotou General Plate Co. Ltd., to produce steel plates in Baotou, Inner Mongolia. (US:51%-PRC:49%). $90 million. 10/04.

GKN Sinter Metals, Inc., a subsidiary of GKN plc (UK)/Shanghai Volkswagen Automotive Co., Ltd.
Signed letter of intent forming joint venture to produce powder metal components for China's auto and industrial markets. 09/04.

OTHER

Nihon Parkerizing Co. Ltd. (Japan)/Shanghai Baosteel Group Corp.
Signed technical agreement to boost cooperation in the research of steel surface treatment chemicals. 09/04.

Petroleum, Natural Gas & Related Equipment

CHINA'S IMPORTS

L'Air Liquide SA (France), Air Products and Chemicals, Inc. (US)
Formed joint venture to supply bulk gases to Beijing BOE Optoelectronics Technology Co. Ltd. (France:50%-US:50%). $30 million. 11/04.

Socotherm Group (Italy)/Chinese Petroleum Pipe Coating Engineering Co., a unit of the China Petroleum Pipeline Bureau

Formed joint venture to provide anti-corrosion pipe coating for the Guangdong LNG Trunkline Project. (Italy:50%-PRC:50%). $11 million. 10/04.

INVESTMENTS IN CHINA

Total SA (France)/Sinochem (Beijing)

Formed joint venture to open and operate 200 gas stations in Beijing, Hebei, Liaoning, and Tianjin. (France:49%-PRC:51%). $120 million. 10/04.

UMW ACE (Labuan) Ltd., a subsidiary of UMW Holdings Bhd. (Malaysia)

Will buy 51% stake in Jiangsu-based Wuxi Seamless Oil Pipe Co. Ltd. $33 million. 10/04.

Pharmaceuticals

INVESTMENTS IN CHINA

Novartis AG (Sweden)/Shanghai Institute of Materia Medica

Formed joint venture to refine and develop traditional Chinese herbal medicines. $1.5 million. 11/04.

Rail

CHINA'S IMPORTS

Midas Holdings Ltd. (Singapore)

Won contract to supply China Northern Car Group Qiqihaer Railway Car Co. Ltd. with aluminum alloy profile structures for use in manufacturing freight train cars. $1.4 million. 11/04.

Midas Holdings Ltd. (Singapore)

Won contract to provide aluminum alloy profile structures to China Southern Car Group Beijing 27 Factory for use in manufacturing freight train cars. $1.4 million. 11/04.

Midas Holdings Ltd. (Singapore)

Won contract to provide aluminum alloy profile structures to Baotou Northern Chuangye Co. Ltd. for use in manufacturing freight train cars. $1.3 million. 11/04.

Midas Holdings Ltd. (Singapore)

Won contract to provide aluminum alloy profile structures to China Southern Car Group Zhuzhou Car Factory for use in manufacturing freight train cars. $1.1 million. 11/04.

Nabtesco Corp. (Japan)

Received order to supply brake systems for 480 railroad cars in China. $47.3 million. 11/04.

Bombardier Inc. (Canada)

Signed a procurement contract to supply 48 subway cars to Guangzhou Metro Corp. $71 million. 10/04.

Bombardier Inc. (Canada)

Received order, through its Bombardier Sifang Power (Qingdao) Transportation Ltd. joint venture from the Ministry of Railways for the production and delivery of 20 eight-car high-speed train sets. $263 million. 10/04.

Alstom SA (France)

Won contract to provide 16 complete subway trains to Shanghai Shentong (Group) Co. Ltd. $160 million. 10/04.

Research & Development

INVESTMENTS IN CHINA

France Telecom SA

Established its first wholly owned R&D facility in Beijing's Zhongguancun. $3.8 million. 11/04.

Royal Philips Electronics NV (the Netherlands)

Established an R&D center in Shanghai. 11/04.

Townsend Polymer Services and Information (US)/All China Marketing Research Co. Ltd. (Beijing)

Formed strategic alliance to create database of China's plastic resin processing facilities. 11/04.

Cisco Systems, Inc. (US)

Will open R&D center in Shanghai. $32 million. 09/04.

Retail/Wholesale

INVESTMENTS IN CHINA

BP plc (UK)/Sinopec

Formed retail joint venture to build, operate, and manage 500 service stations in Hangzhou, Ningbo, and Shaoxing, Zhejiang. $265 million. 11/04.

Fuji Xerox Co. Ltd. (Japan)

Will establish a direct sales network and training facility in China. $300 million. 11/04.

SPAR International (the Netherlands)/Jia Jia Yue Supermarket Co. Ltd. (Shandong)

Signed license agreement for the creation of 15 new SPAR hypermarkets in Shandong. 11/04.

Toshiba Corp. (Japan)/TCL Corp. (Guangdong)

Will form joint venture to sell home appliances in China. (Japan:49%-PRC:51%). $4.6 million. 11/04.

Telecommunications

CHINA'S EXPORTS

Huawei Technologies Co., Ltd. (Shenzhen)

Won contract from Kenya's Safaricom Ltd. to reconstruct and update its network. $34 million. 11/04.

Huawei Technologies Co., Ltd. (Shenzhen)

Won contract to provide GSM base stations to Vmobile Nigeria Ltd. $80 million. 11/04.

Huawei Technologies Co., Ltd. (Shenzhen)

Won contract to provide network expansion and optimization solutions to Zimbabwe's TelOne. $288 million. 11/04.

Huawei Technologies Co., Ltd. (Shenzhen)

Won contract to provide GSM systems and services to Zimbabwe's NetOne. $40 million. 11/04.

ZTE Corp. (Shenzhen)

Won contract to supply Hungary-based Invitel Rt. with advanced ADSL modems. 09/04.

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The *China Business Review*, the official magazine of the US-China Business Council, is the leading authority on China trade and investment. Published since 1974, the *CBR* offers you:

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THE CHINA BUSINESS REVIEW

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"The *China Business Review* is a must-read update on news and trends shaping the US-China business relationship."

—Sean Maloney
Executive Vice President
Intel Corporation

"The *China Business Review* consistently provides timely and useful information and insights from knowledgeable contributors, which we find relevant to our interest in commercial and political developments in US-China relations."

—Vaughn Koshkarian
President, Ford Asia Pacific Operations and Vice President
Ford Motor Company

ZTE Corp. (Shenzhen)
Won contract to provide its wireless local loop network to the Saudi Telecom Co. (Saudi Arabia). 09/04.

ZTE Corp. (Shenzhen)
Won second phase of a CDMA 2001X network construction project in Vietnam. 09/04.

CHINA'S IMPORTS

Cisco Systems Inc. (US)
Will provide equipment for the China Telecom IP Next Generation network and the backbone network in Anhui, Fujian, Hubei, Jiangsu, Jiangxi, and Zhejiang. 11/04.

Compagnie Financière Alcatel (France)
Won contract to provide DSL services to Shaanxi Telecom, a subsidiary of China Telecom. 11/04.

Siemens AG (Germany)
Won contract to expand China Mobile's wireless network. 11/04.

Siemens AG (Germany)
Won contract to expand China Unicom's wireless network. 11/04.

AGS Pte Ltd., a subsidiary of Autron Corp. Ltd. (Australia)
Signed three-year agreement to provide equipment and preventive maintenance services to Hangzhou Eastcom Cellular Phone Co. Ltd. $20 million. 10/04.

Lucent Technologies Inc. (US)
Won contracts to expand CDMA2000 solutions to China Unicom's mobile networks in Liaoning, Shaanxi, and Zhejiang. $107 million. 10/04.

UTStarcom, Inc. (US)
Will expand the metropolitan area network of China Mobile in Tianjin. 10/04.

UTStarcom, Inc. (US)
Won contract from China Netcom Corp. to expand its PAS network to 11 cities in Hebei. $37 million. 10/04.

Alvarion Ltd. (Israel)
Will expand China Netcom's wireless network in Hunan, Jiangsu, Sichuan, and Zhejiang. 09/04.

Array Networks, Inc. (US)
Will help secure Tencent Group's corporate intranet. 09/04.

DMX Technologies Group Ltd. (Singapore)
Won contracts from China CATV (Sichuan), China Unicom (Beijing), and China Telecom (Guangdong) to provide digital video solutions, mobile information centers, and cyber defense security solutions, respectively. $2.6 million. 09/04.

Nokia Corp. (Finland)
Signed contract with Jiangxi Mobile Communications Corp. Ltd. to expand its GSM network. $60 million. 09/04.

Nortel Networks Corp. (Canada)
Selected by China Telecom to provide optical systems to expand its networks in Changsha, Hunan; Chongqing and Chengdu, Sichuan; Fuzhou, Fujian; Guangzhou, Guangdong; Nanjing, Jiangsu; Shanghai; Wuhan, Hubei; Hangzhou, Zhejiang; Hefei, Anhui. (9/04)

Unity Wireless Corp. (Canada)
Won bid to supply ZTE Corp. with additional power amplifiers. 09/04.

INVESTMENTS IN CHINA

Alcatel (France)/Datang Telecom Technology Co., Ltd. (Beijing)
Agreed to jointly develop TD-SCDMA in China. $32 million. 11/04.

P-com, Inc. (US)/Nanjing Putian, a subsidiary of China Putian Corp. (Beijing)
Formed joint venture, Beijing P-Com Broadband Wireless Communications Ltd., to market P-Com's wireless products to large mobile carriers and corporate customers in China. 10/04.

STMicroelectronics NV (Switzerland)/Shanghai High Definition Digital Innovation Ltd.
Formed joint venture to develop, market, and sell digital TV software. (Switzerland:65%-PRC:35%). 10/04.

Textiles & Apparel

INVESTMENTS IN CHINA

Daiwabo Rayon Co. Ltd., Sojitz Holdings Corp., Tomen Corp., Toyota Tsusho Corp. (Japan)/Qingdao Jifa Group
Will form joint venture, Qingdao Jifa Longshan Dyeing and Weaving Co., to produce textiles for high-quality shirts and trousers in Shandong. (Japan:35%-PRC:65%). $20 million. 11/04.

OTHER

Linmark Group (Hong Kong)/China Textile Information Center
Selected by China National Textile Industry Council to jointly develop and promote a Code of Conduct governing environmental and labor standards in China's textile industry. 10/04.

Invista (US)
Will build spandex fiber plant in Foshan, Guangdong. 09/04.

CBR 2004 Readership Survey Results

Who are *CBR* readers? And why do they read the *CBR*? Survey says...

Are you an upper-level executive in a US-based manufacturing company with decision-making responsibility over your firm's China operations? In connection with this responsibility, do you make more than seven trips to China and elsewhere in Asia every year? If so, you are like many of your fellow *CBR* readers.

You may also spend half an hour to an hour reading every issue of the magazine and spend most of that time reading the *CBR*'s special focus and feature articles, the China Business listing of recent Sino-foreign business deals, or our statistics pages. You probably enjoy our articles on China's economy and political situation, government relations, or your industry.

So says the *CBR*'s 2004 Readership Survey. During the summer of 2004, Illinois-based Research USA, Inc. undertook a study for the magazine that surveyed nearly 1,000 *CBR* readers, two-thirds of whom were also members of the US-China Business Council (publisher of the *CBR*) (see p.49). Forty percent of the surveys were returned; the results yielded invaluable information and thoughtful comments that will enable us to better serve our readers (and will help the Council serve its members). Highlights of the survey results follow.

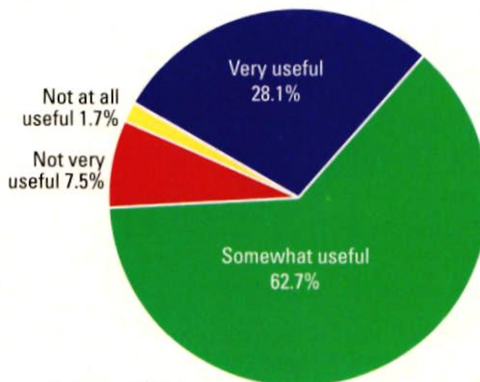
Why read the *CBR*?

Though we are well aware that our most enthusiastic readers were more likely to complete the survey, we were still gratified that 90 percent of survey respondents said they find the magazine "very" or "somewhat" useful (see Figure 1). Of those, 81 percent read the magazine "to keep abreast of the latest developments" and 56 percent said they read it "to gain insight into the thinking of US/PRC leaders" (see Table 1). Almost half read the *CBR* for long-term strategic planning, and more than 40 percent read it to "learn more about market opportunities."

China's economy and political situation were topics of "strong" or "moderate" interest to more than 90 percent of respondents. Almost 90 percent were interested in our

Catherine Gelb
is editor of the *CBR*.

Figure 1: Usefulness of the *China Business Review* as a Source of Information



Source: Research USA, Inc.

Table 1: Why Read the *China Business Review*?

Reason	Percent
To keep abreast of the latest developments	81.0%
To gain insight into the thinking of US/PRC leaders	56.0%
For long-term strategic planning	46.8%
To learn more about market opportunities	41.5%
To identify potential business partners and/or prospects	14.0%
To track competitors	11.5%
Other	5.9%

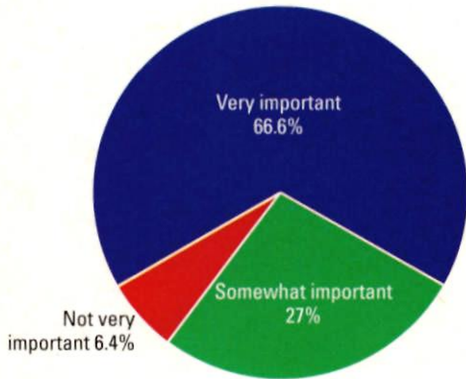
Note: Respondents could choose more than one reason.
Source: Research USA, Inc.

"...a good, current source of competitive intelligence that can be used as collateral information to confirm other sources."

"We would like more sophisticated and in-depth analysis and reporting."

"I have appreciated *China Business Review* over the last couple of decades."

Figure 2: Importance of China Market to Respondents' Businesses



Source: Research USA, Inc.

articles on government relations, and 80 percent were strongly or moderately interested in our articles on investment and trade. Legal issues, manufacturing, human resources, and individual sectors such as telecom and sales and marketing also registered strongly with respondents (see Table 2). Maybe this level of interest accounts for the fact that two-thirds of respondents said they either save every copy of the *CBR* or pass it on to their colleagues.

Table 2: Topics of Interest to *CBR* Readers (%)

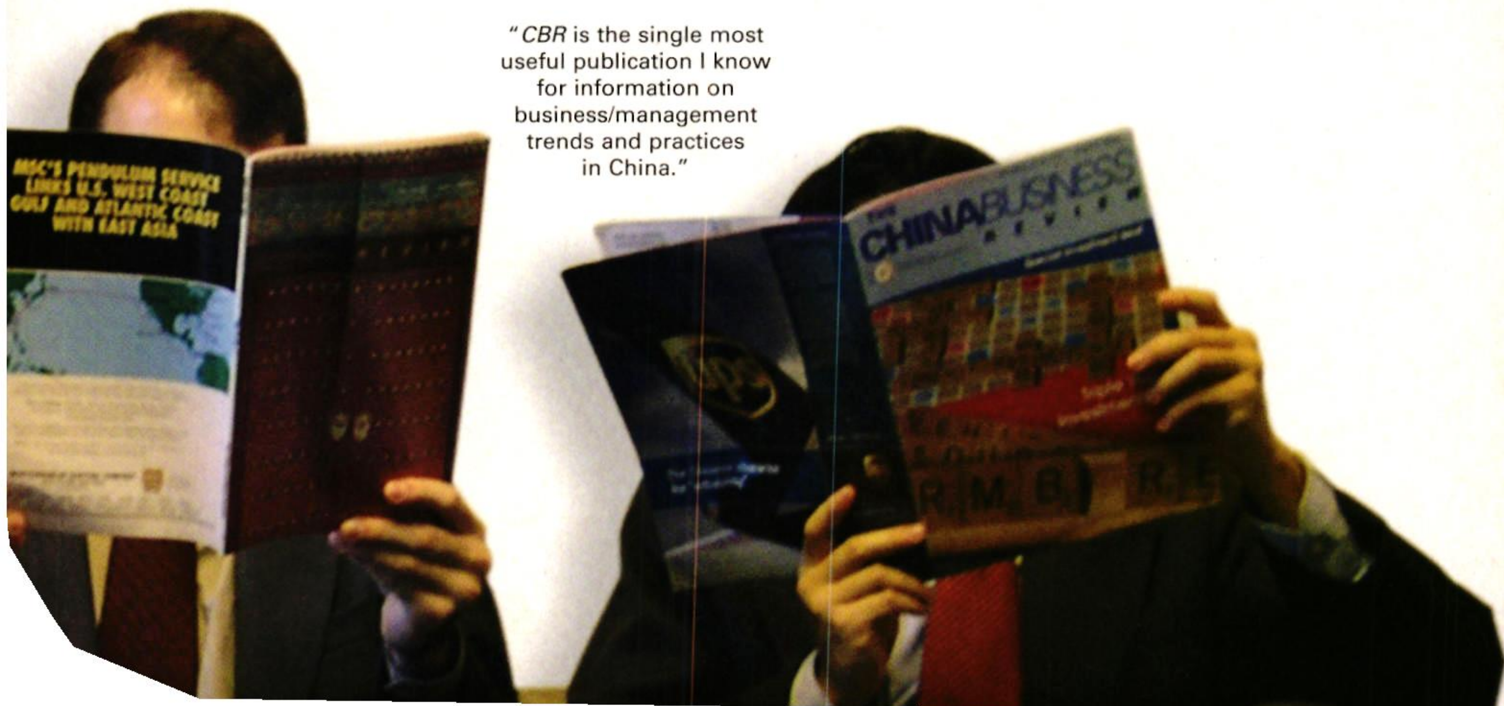
	Strong interest	Moderate interest	Little interest	No interest
Economy/politics	56.6	34.6	7.3	1.5
Government relations	49.0	40.1	9.5	1.4
Investment in China/import/export	45.7	35.9	14.1	4.3
Legal	38.5	40.0	17.8	3.7
Manufacturing	34.9	34.9	21.1	9.1
Sales & marketing	31.5	37.0	22.3	9.2
Transportation/logistics/ distribution/retailing	30.6	32.3	28.9	8.2
Telecom & information technology	20.3	32.3	33.4	14.0
Human resources	19.2	43.3	27.3	10.2
Administration/general management	16.4	49.3	26.1	8.2
Raw materials	16.2	28.2	36.8	18.8

Source: Research USA, Inc.

Table 3: *CBR* Survey Respondents' Businesses

Manufacturing	37.3%
Legal services	10.9%
Business services	7.0%
Banking/finance/insurance/real estate	5.0%
Telecom	4.5%
Education	4.2%
Transportation	3.9%
Retail/wholesale	3.6%
Construction/engineering	3.3%
Health/medical/pharmaceutical	3.1%
Utilities	0.8%
Nonprofit/association	0.8%
Government	0.6%
Hospitality/entertainment	0.3%
Other	14.7%

Source: Research USA, Inc.

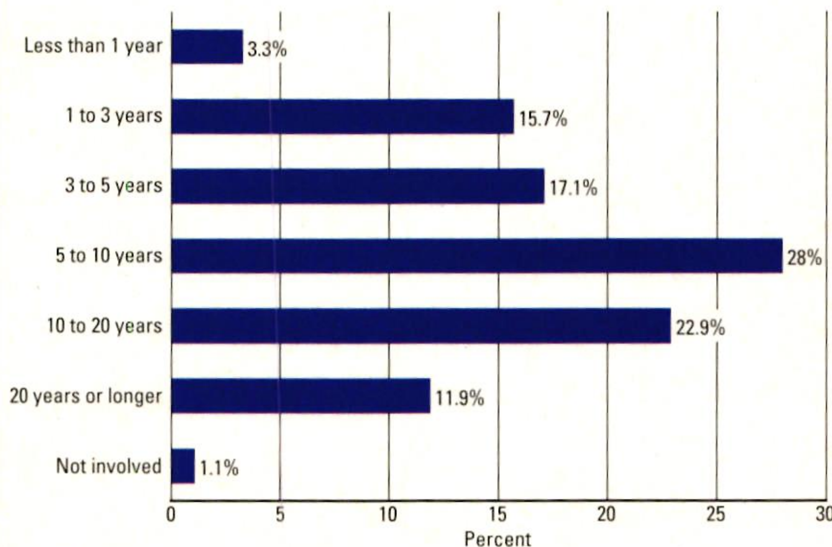


"*CBR* is the single most useful publication I know for information on business/management trends and practices in China."

In good company

Almost 40 percent of *CBR* reader survey respondents work for manufacturing firms, while the others work in services such as law, finance, and consulting (see Table 3). Two-thirds of readers said that China is "very important" to their companies; 27 percent said it was "somewhat" important (see Figure 2). Readers are generally chief executive, operating, or financial officers; directors, managers, or vice presidents; or owners or partners who have been involved in China business for more than 10 years (see Figure 3).

Figure 3: *CBR* Readers' Experience in China



Source: Research USA, Inc.

Research USA, Inc. reports that most of these executives are responsible for administration and general management, government relations, sales and marketing, and investment in China (see Table 4). More than half develop, implement, or oversee corporate China strategy, and just under half plan and develop joint ventures or strategic alliances, manage relations with strategic partners, or are involved in contracts and negotiations for new projects. According to the survey, an average of 1,268 employees work for *CBR* readers' companies in China—though the median is a more modest 142 employees (see Figure 4).

Frequent fliers

It is no surprise that *CBR* readers are frequently on the move, if only because two-thirds are based in the United States (and most respondents' companies are US-based) and yet have China responsibilities. More than 90 percent of respondents took at least one trip out of their country base between summer 2003 and summer 2004; the average number of trips was more than seven, mostly to and from China and Hong Kong—passing through about three cities each trip. A majority of respondents said they fly business class (often on United Airlines) during these trips. On average, *CBR* reader survey respondents spent 46 nights in a hotel in the previous year.

"Make it fun!"

The *CBR* is already considering respondents' suggestions for topics to cover more (or less) often, and new formats. For example, some respondents asked for articles on China's railways, tourism sector, media and entertainment, foreign relations, and politics. Many readers expressed a lack of interest in articles on general management/administration and raw materials. As for format suggestions, we had several requests for more case studies and for more "light" pieces about life in China. One respondent asked us to publish monthly to keep on top of the rapidly changing events in China. Another asked us to double our size. We'll have to think carefully about those two.

We hope our readers will notice some changes in the coming months based on these suggestions. For those of you who did not have a chance to participate in our survey, please do not hesitate to write to us directly (publications@uschina.org) with suggestions for ways to better inform you about the China market. 宪

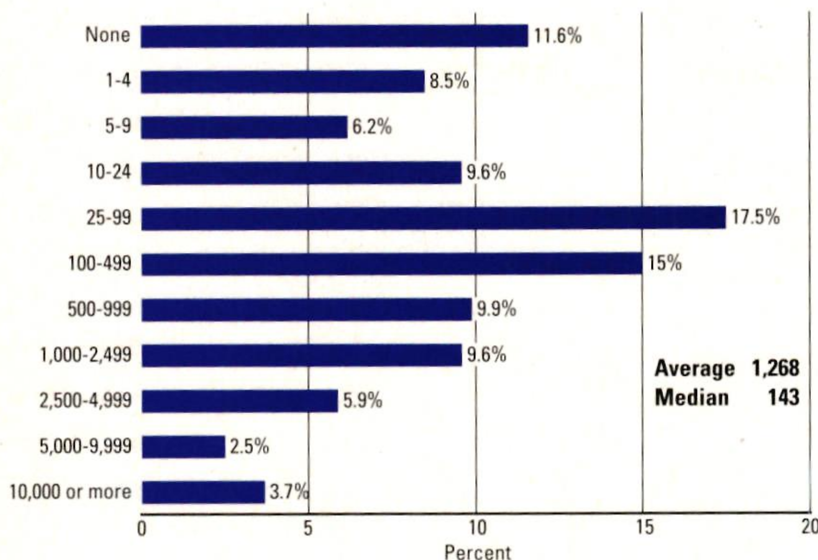
Table 4: *CBR* Reader Survey Respondents' Responsibilities

Responsibility	Percent
Administration/general management	37.0%
Government relations	34.5%
Sales and marketing	32.2%
Investment in China	29.1%
Legal	26.3%
Personnel	25.1%
Import/export	22.0%
Manufacturing	21.5%
Consulting services	20.6%

Note: Respondents could choose more than one area of responsibility.

Source: Research USA, Inc.

Figure 4: *CBR* Readers' Employees in China



Source: Research USA, Inc.

Survey Methodology

The 1,000 names used for this survey were selected from the *China Business Review*'s circulation list. Every name selected was mailed an advance notice postcard informing them of the survey and asking for their cooperation. Every name was then mailed a four-page questionnaire, a one-dollar-bill incentive, and a stamped return envelope. Non-respondents were subsequently mailed another copy of the questionnaire, a cover letter, and a stamped return envelope with another dollar-bill incentive. By September 13, 2004, 372 completed questionnaires had been returned, out of a net effective mailing of 953, for a percentage return of 39 percent.

—*Research USA, Inc.*

US-China Business Council Members Weigh In

Two-thirds of *CBR* reader survey respondents were members of the US-China Business Council (USCBC), so the survey included a question asking members to evaluate Council services. We asked respondents to rate the Council's business advisory consulting services, numerous publications, events and conferences, and overall research and analysis on PRC and US regulatory and policy changes.

More than half of USCBC member-respondents rated each of the Council's services "very" or "somewhat" valuable. The Council's business advisory services department, which offers consulting services to members, and the Council's *China Market Intelligence* weekly, members-only, electronic newsletter, were considered "very valuable" by more than a quarter of respondents. The Council's core service, which reaches across all of the organization's departments—"research and analysis on PRC and US regulatory and policy changes"—received the top, "very valuable" rating from 37.6 percent of respondents. The *CBR*, the Council's semi-annual and annual conferences, and the website all were rated "very valuable" by almost 20 percent of respondents.

On the other hand, almost 30 percent of respondents find the Council's annual conferences, Forecast and Annual Meeting in Washington and China Operations in Shanghai, either "not very valuable" or "not at all valuable." Some respondents asked for more events to be held in China and Hong Kong. Almost a fifth of respondents find the Council's business advisory services not very or not at all valuable. Almost a quarter felt this way about the Council's position papers and advocacy work. The Council is taking both the compliments and criticisms into account as it plans its future agenda.

—*Catherine Gelb*

"*China Business Review* could focus more frequently on opportunities for [the] USA's small or medium-sized enterprises in China. Most American companies/people think that only big companies can survive in China—but small companies can too."

CRITICAL EYE ON BEIJING

An ancient capital is poised to make a high-tech leap

Lin Jun

CBR Focuses on Regional Investment Locations

In the next few issues, the *CBR* will be profiling investment environments around China. These reports will be based on information from site visits to industrial zones, interviews with foreign companies, and information from local infrastructure and development plans. The reports will focus on the overall investment, operational, and logistical environments of each city. The goal of the reports is to paint a clearer picture of the growth trends in the many promising investment locations across China.

Beijing has long prided itself on its reputation as the political and cultural capital of China, and with the 2008 Olympic Games around the corner, its economic profile is set to rise. Significant renovations and upgrades of the city's infrastructure and facilities are underway and foreign confidence in Beijing's future is already starting to show: Contracted foreign direct investment (FDI) jumped 120 percent in the first three quarters of 2004 compared to the same period in 2003.

Beijing is pouring investment into three commercial districts: information technology in the Zhongguancun Science and Technology Park; high-tech industries in the Beijing Economic-Technological Development Area; and real estate and services in the Central Business District (CBD), in which the municipal government plans to invest some $1.5 billion. Located around the East Third Ring Road in the China World Trade Center area, the CBD will be Beijing's business center, designed to attract corporate regional headquarters into an area that, the government hopes, will become "China's Manhattan." Other investment plans include further development of the financial district west of Tiananmen, development of a "Media Street" in the Xuanwumen area, development of a tourist area that will extend along the city's north-south axis from the Drum Tower in the north to the Temple of Heaven in the south, and development of an international food street to cover 50,000 m^2 around the Olympic Park.

A capital economy

Beijing is known nationwide as a manufacturing center of communication equipment, computers, and other electronic equipment and is emerging as an auto production base. Beijing also has a longstanding plan to develop the city's services in information technology, real estate, and finance and insurance.

Beijing's GDP grew rapidly in the first three quarters of 2004, up 13 percent over the same period of 2003. The service sector accounts for just under two-thirds of the economy, and manufacturing and construction account for the rest, with high-tech manufacturing contributing nearly 30 percent of Beijing's industrial value-added output.

The municipal government highlights six key areas for development in its industrial plans:

- Electronics and information;
- Auto manufacturing;
- Petrochemicals;
- Equipment manufacturing;
- Biopharmaceuticals; and
- Light industry, including food and beverages, garments and textiles, printing and packaging, and home furniture.

Lin Jun
is a research associate at the US-China Business Council in Beijing.

Beijing Basics

First three quarters of 2004
Population: 14.6 million*
Per capita GDP: $3,823 (+9.2%)*
Average per capita urban disposable income: $1,414.63 (+12.6%)
Average per capita urban spending: $1,100.46 (+12.8%)
Average per capita rural net income: $742.44 (+10.3%)

Economy
GDP: $35.91 billion (+13.0%)
Fixed-asset investment: $18.44 billion (+16.0%)
Value-added industrial output: $10.90 billion (+20.8%)
Retail sales: $19.46 billion (+16.1%)
CPI: +0.7%

Foreign Direct Investment
Number of contracts signed: 1,333 (+32.0%)
Amount contracted: $4.84 billion (+120%)
Amount utilized: $2.56 billion (+50.2%)

Foreign Trade
Total trade: $67.64 billion (+32.4%)
Exports: $14.27 billion (+16.8%)
Imports: $53.37 billion (+37.4%)
FIE exports: $4.98 billion

Note: *Year-end 2003
Sources: Beijing Municipal Bureau of Commerce, Beijing Statistics Bureau, PRC Ministry of Commerce, official press reports

Major Development Zones in Beijing

National-level zones
Zhongguancun Science & Technology Park
www.zgc.gov.cn
Beijing Economic-Technological Development Area
www.bda.gov.cn
Beijing Tianzhu Airport Industrial Zone
www.chinabaiz.com

Municipal-level zones
Central Business District
www.bjcbd.gov.cn
Beijing Financial Street
www.jrjkg.com.cn
Daxing Industrial Development Area
www.dida.net.cn
Beijing Industrial Base of Optical-Mechanical-Electronics Integration
www.bjoip.com.cn

Source: The US-China Business Council

Useful Websites

The City of Beijing
www.beijing.gov.cn
Beijing Municipal Bureau of Commerce
www.bjmbc.gov.cn
Beijing Investment Promotion Bureau
www.investbeijing.gov.cn
The Official Site of the Beijing Olympics
www.beijing-2008.org
Beijing Investment Platform
www.bjinvest.gov.cn

Source: The US-China Business Council

Most foreign investment has gone into services and export-production in Beijing: foreign-invested interprise (FIE) exports reached $4.98 billion in the first three quarters of 2004, accounting for over 30 percent of Beijing's total exports. Investment in service industries accounted for 60 percent of Beijing's contracted FDI. Investment in wholesale and retail, computer services, and information consulting services rose about 40 percent each in 2003, while investment in finance and insurance rose more slowly.

Attracting foreign investment

Beijing remains a popular place for foreign companies to do business. According to the Beijing Investment Promotion Bureau, FIEs employ 500,000 people in Beijing—one out of every 27 citizens. Roughly 300 multinational corporations in China have their head offices in Beijing, accounting for 60 percent of the total head offices nationwide.

Foreign companies are attracted to Beijing by its easy access to government officials and policy formation, highly skilled work force, deep pool of trained managers, and large market for consumer goods and financial transactions. In the past year, many large foreign investors moved to Beijing, including Advanced Micro Devices, Inc., A. Epstein & Sons International, Inc., Autodesk, Inc., Credit Agricole Indosuez, France Telecom SA, Leroy Merlin, PeopleSoft, Inc., and VERITAS Software Corp. And Nokia Corp. announced it would relocate its new regional headquarters, research center, and production base to Beijing in 2005—part of its ambitious plan to restructure its Chinese operations and turn itself into the biggest cell-phone producer and exporter in China. DaimlerChrysler Corp. also announced it would begin to manufacture Mercedes-Benz vehicles in Beijing in July 2005.

But Beijing also has problems that may dampen foreign investment, including air pollution, high costs, transportation bottlenecks, and poor city planning. Like many other Chinese big cities, Beijing is suffering from water and electricity shortages. In August 2004, the municipal government raised water prices by up to 400 percent for industrial and commercial users. Electricity prices are also expected to rise soon.

The city government is trying to improve the investment climate by cutting red tape. It abolished more than 1,000 local rules and regulations and eliminated 70 percent of approval items in 2003. It has also created agencies to help foreign investors, including the Beijing Investment Promotion Bureau (BIPB), previously known as the Beijing Investment Service Center. BIPB offers consulting services and helps foreign enterprises handle establishment, alteration, or termination procedures. The Beijing Municipal Commission of Development and Reform (BMCDR) launched the "Invest Beijing" website to provide comprehensive investment consulting and promote BMCDR projects.

Navigating through Beijing's bureaucracy can be difficult, however, primarily because each district competes for investment. Such competition

has, in the past, led to redundancy and limited cooperation in infrastructure planning, but may be overcome by the need for systems integration and coordination in Olympics planning. Coordination has already improved somewhat since Mayor Wang Qishan took office in April 2003.

Compared with other Chinese cities, such as Shanghai and Guangzhou, Beijing has failed to foster a surrounding economic belt that can provide it with space and support for long-term development, impairing its ability to compete. Lack of sea access has also weakened its investment competitiveness. In addition, Beijing's local government, directly under the central government's watchful eye, is unable to offer some of the preferential policies that other cities readily offer foreign investors. As a result, Beijing has dropped behind Shanghai in attracting regional headquarters.

Promising areas for investment

● **Infrastructure** Beijing will invest $34 billion in the construction of local infrastructure by 2008. In September 2003, the Beijing municipal government issued a regulation that encourages foreign investors to conduct chartered operations in infrastructure facilities—including water, gas, and heating supply; sewage treatment; and solid waste disposal. Foreign investors can also participate in the construction of public transport infrastructure, such as highways, subways, and light rail.

● **City transportation** Beijing's long-term goal is to develop a "New Beijing Transportation System" with special emphasis on public transportation. By 2008, the city plans to complete the fifth and sixth ring roads, 43 km of light rail, and six new subway lines, at a reported total cost of nearly $11 billion. Beijing Capital Airport plans to add a third terminal and runway, as well as 94 new aircraft parking bays. In addition, Beijing is planning to build the capital's second international airport and open it in 10 years, according to press reports.

● **Electronics and information technology** Beijing is already the center of a robust software industry. Over the next few years, the city will focus on the development of six key fields: digital TV, mobile communications, integrated circuit card and electronic identification, computers and networks, auto electronic products, and digital photography.

● **Environmental cleanup** Beijing leaders have pledged that by 2008, 75 percent of the city's energy consumption will come from natural gas and other more environmentally friendly sources, including thermal energy, in which Beijing plans to invest $1.8 billion. The city will establish green belts and will move heavy industry beyond city limits, so that only 7 percent of the downtown area will be devoted to industrial use by 2005. The city also promises that 80 percent of its taxis will run on natural gas by 2008.

The foreign investment tide stimulated by the 2008 Olympic Games will continue to drive Beijing's growth in the years to come, but to better leverage this opportunity the city has to find ways to address its own problems. A key question will be whether the government will improve interagency coordination and governance. Beijing's long-term success depends on it. 完

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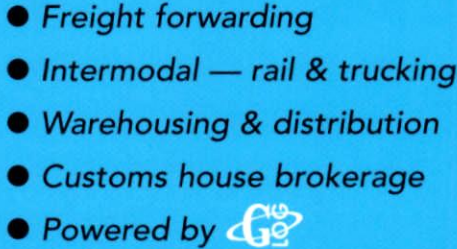

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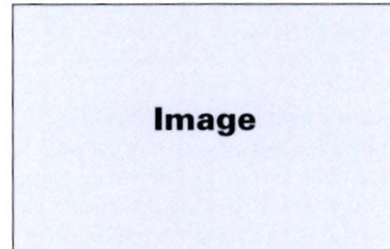

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How to Fly a Cat Back and Forth to China

Vanessa Sterling

Tucker came into my life in March 1995. At the time I was in Beijing studying Chinese and beginning to investigate archives for my dissertation. A self-labeled "crazy cat person," I had spent two months walking through markets looking at free tabby kittens, expensive pure-bred Chinese Persians (*bosi mao*), and all sorts of animals that I still haven't identified. It started as a bet to myself—could I actually adopt a cat in China, make sure it was healthy, and get it on a plane and through Customs on both ends?

After a flurry of faxes to the US Embassy and my sister in Chicago—my intended port of entry—I discovered that the process was not only possible, but should be easy. So one Sunday afternoon, I took a minibus to the now-defunct Xizhimen Bird and Fish Market, hopped out, and in three minutes I was in love. There was the future Tucker: a tiny, slightly grubby, six-week-old white kitten with bright blue eyes and a pink nose, cowering in the back of a cage. When I asked what kind of cat it was, the seller assured me that it was a female, pure-bred *bosi mao*—very healthy and ready to go home. Looking at the cat I knew maybe 35 percent of this was true, but I paid ¥100 ($12) anyway and walked away.

Tucker and I lived happily on the west side of Beijing until late May of that year. His veterinarian was convinced Tucker came to me malnourished, so she told me to feed him as much as possible. She also confirmed my suspicion that he was stone deaf. Oblivious to his disability, he grew like a weed.

I was then confronted with the task of getting him home. I began with airline logistics—coordinating a reservation for him and getting the airline to ship over a US-approved carrier for the cargo hold. They assured me that all would work well unless it was over 85 degrees in Tokyo (in June), where we were scheduled for a four-hour layover. I then investigated arrangements with PRC Customs—which was even easier, once I found the quarantine office hidden among construction sites by the Asian Games Village. Indeed, all I had to do was pay ¥700 ($85), consent to Tucker receiving a rabies shot, and wait for the documents to be typed. (Bear in mind that these documents are only valid for 14 days, a restriction that airport Customs officials strictly enforce.)

Getting through US Customs was even easier. In 1995, all animals had to ride in the hold for international flights, so I claimed him in O'Hare Customs and brought him to the US Department of Agriculture representative. This thoroughly unenthusiastic man looked into the cage for two seconds, stamped my paperwork, and sent us on. We were in the clear.

Since the US trip was so easy, I did not question Tucker's fate when I returned to Beijing in 1997 for field work. He was coming. Starting with the airlines, I realized that rules had changed in our favor. Tucker could now ride in the cabin with me. All I needed was a health certificate from Tucker's vet.

The first problem arose when the vet did not put his name stamp on the certificate, leaving a large blank white area on the form. Knowing that any Chinese would realize the mistake, without even being able to read English, I solved this by using my father's secretary's incoming mail stamp. No worries.

The second problem occurred when Tucker had an adverse reaction to the tranquilizer our vet had given me. Instead of becoming relaxed, Tucker became paranoid and bit my hand with full force when the security guard "helped" me get Tucker back into his carrier after going through security. Bleeding and flustered, I said goodbye to my parents and got on the connecting flight to Detroit. Shortly into our trans-Pacific flight Tucker gave in to the drugs and fell fast asleep.

The third problem happened when my hand ballooned during the flight in reaction to being seriously chomped by an angry 16-pound cat. It throbbed and turned purple, thus assuring me that my first task the next day would be to visit the Beijing International Medical Center for an antibiotic. Finally we landed, and I cashed enough traveler's checks to pay the ¥1,000 ($121) Customs fee for the cat. The inspector looked into the cage, said "Yep, it's a cat," took my money and Tucker's health certificate (the fake "stamp" was accepted), wrote down my address, and assured me that Customs would make a home visit within a month or so.

Customs never came. After my arrival in mid-September their office called me once in late November to set up a home visit. Since they wanted to visit on Thanksgiving Day—and I had dinner plans—I explained that I was busy. They never called again, and Tucker was thus successfully "repatriated."

Our return to the United States in August 1999 was even easier. We went to the same office to get his papers, got on the plane, and when we landed in Detroit the Agriculture representative was on a break—so no inspection at all.

Tucker is none the worse for wear and still plugs along. He's nine now, going blind in addition to his deafness, and approaching 19 pounds. He still loves *baozi* (steamed, stuffed buns) and still reminds me of Beijing everyday. He is the best souvenir I could have. 完

Vanessa Sterling
is completing a doctorate in Chinese History at the University of Pittsburgh.

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